APPENDIX A

United States Court of Appeals

FOR THE THIRD CIRCUIT

No. 12,568

SHELL OIL COMPANY,
Petitioner,

v.

FEDERAL POWER COMMISSION,
Respondent,

TEXAS GAS TRANSMISSION CORPORATION,
Intervenor,

and

LOUISVILLE GAS & ELECTRIC COMPANY,
Intervenor.

ON PETITION TO REVIEW AN ORDER OF THE FEDERAL POWER COMMISSION

Argued October 6, 1958

Before:
GOODRICH, McLAUGHLIN and STALEY,
Circuit Judges.

OPINION OF THE COURT

(Filed January 27, 1959)

By McLAUGHLIN, *Circuit Judge.*

This case is another in that line wherein the issue has been the effective rate on June 7, 1954 for natural gas sold by a so-called independent producer. That date was when the Supreme Court announced its decision in Phillips Petroleum Co. *v.* Wisconsin, 347 U. S. 672 (1954). The effect of

that decision was to subject independent producers of natural gas to regulation by the Federal Power Commission. The Commission, in implementing the decision, called for filing of rate schedules setting forth "* * * rates * * * effective on June 7, 1954."

What that rate was for Shell Oil Company in its contract with Louisiana Natural Gas Company[1] depends upon the contract-established provisions rather than on the fortuity of rates which were being actually paid on that date. See Natural Gas Pipeline Company *v.* Federal Power Commission, 253 F. 2d 3 (3 Cir. 1958), cert. den. 357 U. S. 927 (1958). The contract had been entered on May 1, 1951 and for the period in question provided for the sale of gas at 8.997¢ per Mcf, unless "* * * at any time after December 31, 1951, Buyer [Louisiana] * * * [should] enter into a contract providing for the purchase by it of gas * * *" produced and delivered within a fifty mile radius of any delivery point specified. In that event the contract price was to escalate to the same price as that called for by the subsequent contract with the other producer.

Louisiana had already succeeded to rights as purchaser under a contract entered with Atlantic Refining Company, another producer, in 1943. Under that contract buyer agreed to buy specified daily quantities of gas; it was provided that the rights of the parties should continue for the producing life of the field involved but for not more than twenty-five years. In that contract the buyer agreed to pay 2.2¢ net per Mcf for gas received for the first five years. No fixed price was established for periods after that, but rather the contract provided:

> "(b) At the end of the first five-year period, Buyer and Seller are to reach an agreement as to the price for gas sold and delivered under this contract during the second five-year period. The price

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[1] Louisiana Natural Gas Company was a subsidiary of Texas Gas Transmission Corporation. On June 30, 1955 it was merged into the parent corporation.

to be paid during such second five-year period is to be agreed upon at the beginning of such period after a survey of prevailing prices for gas being sold in similar quantities in the southwestern part of Louisiana.

"(c) During succeeding five-year periods, price to be paid will be determined at the beginning of each period in the same manner as provided for in paragraph (b) above.

"(d) In the event that the parties are unable to agree upon the price to be paid for gas after the first five-year period, in accordance with the arrangements set forth in paragraphs (b) and (c) above, such determination shall be submitted to arbitration in accordance with Condition XII."[2]

A price for the second five year period had been agreed to by negotiation between the buyer and seller, but this agreement expired on August 31, 1953. Louisiana and Atlantic

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[2] Condition XII reads:

"* * * The party desiring such arbitration shall notify the other and in such notice shall name an arbitrator, (sic) the arbitrator to be appointed by the other party shall be named within ten (10) days after receipt of such notice of arbitration, and an additional arbitrator shall, within ten (10) days of the appointment of the second arbitrator, be selected by the two (2) arbitrators theretofore appointed, but if one of said parties shall have failed to appoint an arbitrator within the time provided herein, it is expressly understood and agreed that the sole arbitrator shall arbitrate the question alone. If arbitrators shall have been appointed by the respective parties and shall have failed to select the third arbitrator within the above stated time, the third arbitrator shall be appointed by the senior Judge of the 5th Federal Judicial Circuit upon application therefor by either of said parties to the arbitration.

"* * * The decision in writing signed by a majority of the arbitrators shall be final and conclusive with respect to the matter submitted and the parties hereto agree to accept and abide by the same."

undertook negotiations in September of that year for agreeing to a price for the third five year period.

The parties had difficulty in agreeing. The negotiations consumed five and a half months, finally culminating in an agreement dated February 17, 1954, whereby the price was established at 12.5¢ per Mcf, plus gathering tax. Shell thereafter accidentally learned of this and subsequently notified Louisiana that it felt entitled under its contract to an escalation of its price to the same 12.5¢ level.

There is no dispute that the fifty mile radius requirement of the Louisiana-Shell contract is satisfied. The argument concerning Shell's right to a higher price turns on whether the Louisiana-Atlantic agreement of February, 1954 was an "entering of a contract" which activated the price escalation clause of the Louisiana-Shell contract.

When Shell filed its rate schedule with the Federal Power Commission pursuant to the Commission's orders implementing the Phillips decision, the Commission neither accepted or rejected the submitted rate, pending further explanation by Shell of why it claimed 12.5¢ per Mcf. Shell presented that explanation in February, 1957 when it filed for an increase in rate to 16.75¢ per Mcf. The reasonableness of that rate is still awaiting hearing. The Commission at this point directed that a hearing be held to determine the effective rate on June 7, 1954 under the Shell contract which it simultaneously accepted for filing.

As a result of the hearing the examiner found the effective rate to be 12.5¢. This finding was subsequently reversed on November 12, 1957, by the Commission whose decision is here on appeal by Shell.

The clause in the Louisiana-Shell contract which is central to this controversy is one of the type commonly referred to in the trade as a "most favored nation" clause. The usual objective of such a clause is to assure the seller a top price for its gas. Testimony at the hearing before the Commission's examiner was that Louisiana had desired a twenty year contract which was for a term longer than

Shell had at that time ever contracted for, at least in that area. Because of difficulty in establishing a price for so long a period, the clause in question was agreed upon. It appears that at the time of contracting Shell knew Louisiana was purchasing gas from Atlantic but was not familiar with the specific terms of that contract. These facts tend strongly to demonstrate that the intention of the parties was for any higher price paid by Louisiana to another producer to trigger a rise on the Shell contract to the same figure except possibly where a pre-existing contract already provided for a settled step-up in price.

If the precise arrangement under the Atlantic contract had been known to Shell, then perhaps Louisiana could argue to more purpose that the wording of the Shell contract (which calls for the "enter[ing of] a contract providing for the purchase * * * of gas") was not intended to trigger escalation following an agreement on price when that agreement was reached under an earlier gas purchase contract which contained a binding agreement subsequently to agree on price. But even then the fact cannot be avoided that, at least for purposes of the favored nation clause, the "entering of a contract for the purchase of gas" has not been accomplished until the price has been established. True, Atlantic was obligated to deliver gas for twenty years from 1943 but, just as important, Louisiana was bound to pay for it. And while there may have been enforceable means for settling the rate of payment in the event the parties could not agree, it would nonetheless be true that it was when the price was finally established, by whatever means, that a contract had thereupon been entered. Actually, if the Louisiana-Atlantic agreement of February 17, 1954, was not an entering of a contract we are at a loss as to how it would be properly and legally characterized. The situation fits best into the rubric of an accord itself taken as satisfaction. See 6 Williston on Contracts, §§ 1841, 1846 (rev. ed. 1938). Both parties gave up their rights under the original contract to proceed to arbitration, prom-

ising on the one side to pay and on the other side to accept the price reached.

To make the date of the accord retroactive to the date of the original agreement-to-agree is, of course, abstractly conceivable; but for a court to attribute that effect to the Atlantic contract and apply it to the Shell contract in the absence of recognition of this possibility in the Shell contract would take the law out of the realm of business practicalities. It is far more in line with the realities of the situation to say that complete performance of the 1943 contract required the parties to enter into subsequent contracts. The entering into one of those subsequent contracts triggered the escalation clause in the Shell agreement.

We have assumed without deciding that the Atlantic contract of 1943 did in fact impose a binding agreement-to-agree on the price for gas in each of the contract's last four five year periods. Thus it has not been necessary to determine the several questions raised in connection with the arguments directed to that phase of the case. Of course if the Atlantic contract of 1943 was not a binding agreement-to-agree, that circumstance alone would place the February, 1954 Atlantic contract fully within the terms of the escalation clause in the Shell contract.

The Federal Power Commission order of November 12, 1957 finding Shell's rate with Louisiana on June 7, 1954 to be 8.997¢ per Mcf will be vacated. Because the escalation called for by the contract requires consideration of other factors in determining whether the price to another supplier was indeed higher, the cause will be remanded for consideration of those factors.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit.

Appendix A

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT.

No. 12,568.

SHELL OIL COMPANY,
Petitioner,

vs.

FEDERAL POWER COMMISSION,
Respondent,

TEXAS GAS TRANSMISSION CORPORATION,
Intervenor,

LOUISVILLE GAS & ELECTRIC COMPANY,
Intervenor.

Judgment.

Present:

GOODRICH, McLAUGHLIN and STALEY,
Circuit Judges.

This cause came on to be heard on the record from the Federal Power Commission, and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the order of November 12, 1957 of the Federal Power Commission be, and it is hereby vacated, and the cause remanded with directions to proceed in conformity with the opinion of this Court.

Attest:

IDA O. CRESKOFF,
Clerk.

January 27, 1959.

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Clerk

Appendix A

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LOUISVILLE GAS & ELECTRIC COMPANY,
Intervenor.

Present:

GOODRICH, McLAUGHLIN and STALEY,
Circuit Judges.

Order.

The petitions for rehearing of Federal Power Commission, Texas Gas Transmission Corporation and Louisville Gas & Electric Company in this case are denied.

By the Court,

McLAUGHLIN,
Circuit Judge.

Dated: March 4, 1959.

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IDA O. CRESKOFF

APPENDIX B

Section 19(b) of the Natural Gas Act

[as it appears in 15 U. S. C. A. §717r(b) (Supp. 1958)]

[Rehearings; court review of orders]

(b) Any party to a proceeding under this chapter aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals [*] of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be transmitted by the clerk of the court to any member of the Commission and thereupon the Commission shall file with the court the record upon which the order complained of was entered, as provided in section 2112 of Title 28. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to

[*] "Circuit court of appeals" was replaced by "court of

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IN THE

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PETITIONERS' REPLY BRIEF

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PETITIONERS' REPLY BRIEF

Petitioners respectfully submit this Reply Brief in response to two contentions in the Brief in Opposition submitted by Shell Oil Company (Shell). Petitioners believe that Shell's other arguments are fully answered by their petition for certiorari and that of the Federal Power Commission (Commission) in No. 170.

1. Shell's Claim That Atlantic Pricing Provisions Are Unique Has No Basis in Fact and Does Not Really Deny the Major Importance of This Case

Shell advances only one argument in its attempt to prove that this case does not present important questions. Shell does not claim that *the "future contract" requirement of its contract* is unusual, but, instead, asserts that *the Atlantic pricing provisions* are so "unique and nondescript" that

the decision below has little or no general significance (Points I and II).*

Many Pricing Provisions in Shell's Own Contracts Are Essentially the Same as Those in the Atlantic Contract

Saving for a moment the point that this assertion blows up out of all proportion minor facets of the case, one need only sample Shell's own contracts on file with the Commission to find numerous examples of price determination clauses which are, with minor variations, the same as that in the Atlantic contract.

At least 28 other such provisions may be found among Shell's own contracts, of which the following are illustrative:

> "For each one thousand (1,000) cubic feet of gas purchased under this agreement during each of the next five (5) year periods, Buyer shall pay to Seller and Seller shall accept as full compensation therefor, *a price which shall be agreed upon* during the year commencing August 29, 1956, for the five (5) year period extending from August 29, 1957 to August 29, 1962, *and a price which shall be agreed upon* during the year commencing August 29, 1961, for the five (5) year period extending from August 29, 1962 to August 29, 1967, or, *upon failure of the parties to so agree upon the price* for each of said five (5) year periods, such price shall be determined by arbitration in accordance with the provisions of Article XVII, *which price shall be based on the then going price for gas of similar quality and quantity being delivered under similar conditions in comparable North Louisiana fields*, but shall not be less than ten

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* Shell has "*been unable to find a single existing other Defense Plant Contract of the type of the Atlantic-Defense Plant Contract of 1943*" (emphasis by Shell), or a single other contract "containing a price agreement clause like that" in the Atlantic contract

cents (10¢)." (Agreement of August 8, 1952 with Interstate Natural Gas Co., Inc., Supp. No. 5 to Shell Schedule No. 57.)

"For the fourth five year period *the price shall be the fair and reasonable value* thereof as of the commencement of said period, *taking into consideration the price then being paid for gas of similar quantity and quality sold for similar purposes in the general area of the Clayton Area*, provided, however, that in no event shall such price be less than 10.0883 cents for each 1,000 cubic feet of gas. Six months prior to the commencement of such period such fair and reasonable value *shall be determined by agreement*, but if the parties *are unable to agree* then by a disinterested appraiser * * *." (Contracts of July 15 and January 25, 1950 with Texas Illinois Natural Gas Pipeline Co., Shell Schedule Nos. 2 and 3.)*

These examples reflect extensive use of such flexible price adjustment clauses throughout the industry.

Shell seems to think that there is some magic distinction between this case and cases involving what Shell considers to be a "true" price redetermination clause, that is, one having two attributes: (1) a price floor and (2) a

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* See also Shell Schedules 21, 41, 61, 62, 69, 75-78, 81, 83, 95, 149, 154, 155, 157-59, 163, 164, 167, 168, 178, 183 and 196. Many schedules use yardsticks such as "fair and reasonable value", "fair market value", "prevailing market price" or "fair, just and reasonable price". Of 186 Shell contracts readily available for examination (out of a total of 211 on file with the Commission) at least 22 have pricing provisions using such terms as "agree", "agreement", "negotiate" or "renegotiate", and at least 22 others use language like "if the parties are unable to agree". Two schedules (21 and 76) do not seem to have any stated price standard whatever. Although time did not permit a survey of every gas purchase contract, a quick check of contracts of other producers confirms that there is nothing "unique" or "nondescript" about these Shell contracts.

"definite" formula to ascertain price, normally the average of the three highest prices being paid (Brief, pp. 9-11).*

The first element relied upon by Shell as an important distinction—whether price might theoretically go down as well as up—is wholly beside the point and represents an exercise in semantics. The academic possibility that there might be a *price decrease* could hardly have anything to do with the opposite question of whether a *price increase* has been triggered under a favored-nation clause in another contract. Whether price can go either of two ways or only one way, the parties still must act to determine the new price.

Shell's second factor, the "definiteness" of the price standard, is a quibble about draftsmanship. Unexplained is Shell's own extensive use of price yardsticks which, as indicated above, do not explicitly require averaging of prices.** Moreover, it is clear that the impact of the

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* If Shell proves anything by this, it is that there is *a substantial degree of uniformity, as well as important differences*, in gas purchase contracts, which highlights the need for that specialized insight which is able to identify essential uniformity, and to discern really significant differences.

** It is not amiss to note that Texas Gas and Atlantic not only applied the Atlantic price yardstick of "prevailing prices" (which, contrary to Shell's argument, the documentary evidence unmistakably shows that they did do)—but in applying the yardstick *they actually did average various prevailing prices*. See Texas Gas and Atlantic exchange of written data in February 1954 introduced by Shell as Exs. 5 and 6 (R. 124-27). The most that can be said for Shell's claim of vagueness in the Atlantic price standard is that it is an echo of Shell's main argument on the merits, namely, that the 1943 Atlantic contract was not legally enforceable beyond the first five years (compare Shell's argument on the merits at p. 17 of its Brief). It is difficult to see how even a lack of any stated price standard would affect the enforceability of the Atlantic contract since, in such a case, a standard such as "reasonable price" would ordinarily be presumed. See *United States* v. *Swift & Co.*, 270 U. S. 124, 141. In any event, Shell does not mention a case cited in our petition (footnote to p. 15) which upholds the definiteness of the yardstick of "prevailing field price", and also notes that a great many oil and gas contracts use similar standards. *Cities Service Gas Producing Co.* v. *FPC*, 233 F. 2d 726, 727, 730 (10th Cir. 1956), *cert. denied*, 352 U. S. 911.

decision below reaches beyond any peculiarity of draftsmanship.*

Shell Does Not Deny that the Court-Found Meaning of the Favored-Nation Clause Could Affect Hundreds of Other Contracts—or that the Proper Standard of Review is a Vital Matter—or that There is a Growing Number of Disputes Over Interpretation of Rate Schedules

By virtue of Shell's narrow approach in discussing the importance of the case, *i.e.*, focusing on only one of its several aspects, Shell strangely enough does not really deny the major importance of the remaining questions. It merely argues that the Court of Appeals was right on the merits and that it had unlimited de novo jurisdiction (Points III and IV, pp. 14-28). Shell seems to have no real quarrel with the following points:

> 1. That the broadly applicable statements made by the Court of Appeals in finding the meaning of *the Shell favored-nation clause* (as distinguished from what was said about *the Atlantic contract*) would affect the "future contract" limitations appearing in hundreds of other contracts, or in over 1 out of every 3 favored-nation provisions in the Gulf Coast area.

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* Even the redetermination clause in the Shell contract which Shell attempts to distinguish from that of the Atlantic contract (Brief, p. 10) is swept in by the broad rationale of the court below: "Both parties gave up their rights under the original contract to proceed to arbitration, promising on the one side to pay and on the other side to accept the price reached." The embracing scope of the decision is also due to the fact that under any kind of price determination clause the parties obviously have to take some action and, in some sense, reach an "agreement." *It is the universal custom in the natural gas industry to record every price determination in a "letter agreement".* See, for example, the "letter agreements" in *Phillips Petroleum Co.* v. *FPC*, 227 F. 2d 470, 471-472, 475 (10th Cir. 1955), *cert. denied*, 350 U. S. 1005.

2. That the proper standard to guide the courts in reviewing administrative interpretations of written instruments committed to regulation, is a matter of great consequence.

3. That there is a large and growing number of proceedings before the Commission involving disputes over the interpretation of gas purchase contracts.*

2. Shell's Theory of De Novo Interpretation Has No Place in the Administrative Process

Aside from the merits, Shell's remaining arguments are directed to whether the reviewing court should make a de novo interpretation of the rate schedule.

Shell believes that the "privately negotiated" origin of the present contracts bars the Commission from bringing its accumulated experience to bear, and that uniformity of decision is best achieved by *de novo* judicial decision (Brief,

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* Since the beginning of June, at least 8 more such proceedings were begun: *Arkansas Fuel Oil Corp.* (Docket No. G-19005); *British-American Oil Producing Co.* (G-19024) *id.* (G-19254); *Sunray Mid-Continent Oil Co.* (G-19090); *Texas Gas Products Corp.* (G-18952); *Texas Hydrocarbon Co.* (G-18951); *Western Natural Gas Co.* (G-18889); *El Paso Natural Gas Co.* v. *Amerada Petroleum Corp., et al.* (G-18900) ("Complaint and Petition for Issuance of Declaratory Order to Terminate Controversies and Remove Uncertainties"). The *El Paso* proceeding brings together a large number of disputes, many arising in other proceedings, which involve hundreds of contracts and scores of producers. The *Western Natural* proceeding is a fifth one raising the instant question about the "future contract" limitation. A further check also brings to light *Atlantic Refining Co.* (G-18753) as presenting the same issue. Thus there are now a total of at least *34 interpretative disputes*, one of which directly involves hundreds of contracts, *and 6 of which appear to involve the meaning of the "future contract"* limitation. See also the proceedings cited in the footnotes at pp. 6-8 of our petition.

pp. 2, 14, 18, 22, 25-28). We suggest that the Court's recent decision in *Pennsylvania R. R.* v. *Day*, 360 U. S. 548 indicates the proper view:

> "We can take judicial notice of the fact that provisions in railroad collective bargaining agreements *are of a specialized technical nature calling for specialized technical knowledge in ascertaining their meaning and application.* Wholly apart from the adaptability of judges and juries to make such determinations, varying jury verdicts would imbed into such judgments varying constructions not subject to review to secure uniformity. Not only would this engender diversity of proceedings *but diversity through judicial construction and through the construction of the Adjustment Board.* Since nothing is a greater spur to conflicts, and eventually conflicts resulting in strikes, than different pay for the same work or unfair differentials, *not to respect the centralized determination of these questions through the Adjustment Board would hamper if not defeat the central purpose of the Railway Labor Act*" (360 U. S. at 553).

We find it hard to understand how Shell can wholly ignore *United States* v. *ICC*, 198 F. 2d 958, 963-64, 975 (D. C. Cir. 1952), *cert. denied*, 344 U. S. 893, which, as we pointed out in our petition (p. 10), conflicts in principle with the present decision, even apart from the *Memphis* case (358 U. S. 103). In the *ICC* case, the District of Columbia Circuit carefully refrained from construing a railroad rate tariff and left the job of interpretation up to the Commission, even though it ruled that the Commission's original interpretation was unsupported and could not stand.

The Commission's Accumulated Experience

Shell's energetic attempt to distinguish the *Memphis* case really falls back upon the unfounded assumptions that the Commission neither has, nor employed here, any specialized knowledge or experience (Brief, pp. 16, 19, 24-26).

Shell nowhere mentions the Commission's expert reliance in its order denying rehearing upon the marked difference in terminology between the present limited favored-nation clause and clauses from other Shell contracts in the record (R. 2151-52).

The Commission's special familiarity with the inner workings of all the segments of the natural gas industry—producers, pipeline companies, distributing companies and consumers—has been obtained from its day to day study of this complex industry over two decades.

Long prior to the 1954 *Phillips* decision this familiarity extended to the practices and needs of gas producers and the provisions employed in gas purchase contracts. For example, in passing upon pre-1954 applications for certificates of public convenience and necessity submitted by the pipeline purchasers seeking to construct required new facilities, it was essential that the Commission determine that the supply of gas originating from the producing fields was adequate to serve the public need.* The Commission's regulations require the pipeline companies to attach copies of their gas purchase contracts as exhibits to their certificate applications. See requirements for what is now "Exhibit H" under Section 157.14(a)(10)(v) of the Regulations under the Natural Gas Act (18 C. F. R.).

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* For instance, in the first major decision on such a pipeline application, the Commission made a careful study of the adequacy of the natural gas supplies and the various forms of the gas purchase contracts, including pricing features. See *Kansas Pipe Line & Gas Co.*, 2 F. P. C. 29, 40-45 (1939).

Prior to 1954, the Commission and its Staff were therefore required to consider thousands of gas purchase contracts of independent producers and became familiar with all types of flexible price adjustment clauses.*

But, this only represents part of the Commission's pre-1954 familiarity with producing problems. For example, the Commission added substantially to its special knowledge about gas production in the *Natural Gas Investigation* (Docket No. G-580), which extended from 1944 to 1948.

Shell's argument that the process of interpreting a gas purchase contract is solely a matter of "law", oversimplifies the question of the proper standard of review and is contradicted by the fact that the Court of Appeals made findings of subjective intention and business "practicalities."

Conclusion.

It is respectfully submitted that the petitions for certiorari should be granted as presenting questions of general importance.

Not only does de novo judicial interpretation raise significant problems in administering the Natural Gas Act, but the decision below emasculates the widely used "future contract" form of restraint on inflation of field prices. Such a result is obviously a matter of serious public concern comparable to that expressed by the Court in *Atlantic Refining Corp.* v. *Public Service Commission*, 360 U. S. 378, 391-92 with respect to the impact on the consumer of the

* Thus, before 1954, both the Atlantic and the Shell contracts had been introduced in evidence in the hearing in Docket No. G-1578.

rising price plateaus in southern Louisiana and the "triggering" of favored-nation clauses.

Respectfully submitted,

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ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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March 4, 1960

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1959

Nos. 167 and 170

FEDERAL POWER COMMISSION, TEXAS GAS TRANSMISSION CORPORATION, and LOUISVILLE GAS AND ELECTRIC COMPANY,
Petitioners,

v.

SHELL OIL COMPANY,
Respondent.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR PETITIONERS TEXAS GAS TRANSMISSION CORPORATION AND LOUISVILLE GAS AND ELECTRIC COMPANY

Opinion and Orders Below

The opinion of the Court of Appeals (R. 160)* is reported at 263 F. 2d 223. The order of the Federal Power Commission (Commission) (R. 126) appears at 18 F. P. C. 617, 22 P. U. R. 3d 94; its denial of rehearing (R. 143) is reported at 19 F. P. C. 74, 22 P. U. R. 3d 101.

* References throughout this brief are to the pages of the Transcript of Record printed for use of the Court.

Jurisdiction

The judgment of the Court of Appeals was dated and entered on January 27, 1959 (R. 165). Timely petitions for rehearing were filed on February 20, 1959 and were denied by the Court of Appeals by order dated March 4, 1959 (R. 166).

By orders of Mr. Justice Brennan dated May 25, 1959, the time for filing petitions for a writ of certiorari was extended to and including July 2, 1959 (R. 167-68). Two petitions for a writ of certiorari were duly filed, one by the Commission and the other jointly by Texas Gas Transmission Corporation (Texas Gas) and Louisville Gas and Electric Company (Louisville). Both petitions were granted on October 12, 1959 and the two cases were consolidated (361 U. S. 811; R. 168-69).

The jurisdiction of the Court rests on 62 Stat. 928, 28 U. S. C. §1254(1) and Section 19(b) of the Natural Gas Act, 52 Stat. 831 (as amended, 72 Stat. 947), 15 U. S. C. §717r(b) (1958).

Statutes Involved

The statutes involved are Section 19(b) of the Natural Gas Act and Section 10(e) of the Administrative Procedure Act, 60 Stat. 243, 5 U. S. C. §1009(e), which are printed in full as Appendices A and B hereto.

Questions Presented

In a contract for the purchase of gas between Shell Oil Company (Shell) and Texas Gas, one of the provisions dealing with price increases was a favored-nation clause

under which the producer, Shell, would be entitled to a price increase should Texas Gas after December 31, 1951 "enter into a contract providing for the purchase by it of gas" at a higher price. Subsequent to December 31, 1951, Texas Gas redetermined price under a pre-existing long-term contract with another producer, The Atlantic Refining Company (Atlantic), which required that the price be so redetermined every five years on the basis of the then-prevailing prices, the redetermined price to be fixed by arbitration should the parties fail to agree. In proceedings under the Natural Gas Act to establish Shell's effective rate, its contract having been filed as a rate schedule, the Federal Power Commission ruled that the price redetermination under Texas Gas' prior contract with Atlantic was not "entering into a contract for the purchase of gas" within the meaning of Shell's favored-nation clause and Shell was therefore not entitled to a price increase. The questions presented are:

1. May a court of appeals, on review of the Commission's order, decide for itself the meaning of the favored-nation clause and make its own evaluation of industry practice and usage and independent findings of fact, or should it accept the Commission's interpretation when reasonably supported?

2. Whether the favored-nation clause of Shell's rate schedule provided for a price increase in these circumstances?

Statement of the Case

The order of the Commission determined the rate effective on June 7, 1954 for sales of gas by Shell. The filing of Shell's contract as a gas rate schedule was required by the Commission's regulations governing independent producers (18 C. F. R. §§154.92-94 (Supp. 1958)), which were issued in accordance with the decision of the Court in *Phillips Petroleum Co.* v. *Wisconsin*, 347 U. S. 672.

A. The 1951 Shell Contract

The gas purchase contract (Item A,* R. 57-71, 152-59) filed by Shell as a rate schedule was entered into as of May 1, 1951 between Shell and Texas Gas.** Shell is an independent producer of natural gas and the seller under the above rate schedule. Texas Gas, an interstate pipeline company, purchases the gas from Shell for resale in interstate commerce. Both Shell and Texas Gas are "natural gas companies" within the meaning of and subject to the Natural Gas Act.***

The favored-nation provision here in issue reads as follows:

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* Citations to an "Item" refer to certain documents filed with the Commission, introduced in evidence through incorporation by reference. "Ex" is used to designate exhibits physically put into evidence. Record references are limited to the place in the record where the document or its pertinent provision appears. Generally, the portions of the record which were printed do not include the transcript page at which the document was offered in evidence.

** Shell originally contracted with Louisiana Natural Gas Corporation, a wholly owned subsidiary of Texas Gas. For convenience, "Texas Gas" refers throughout this brief both to the parent company and its subsidiary.

*** Louisville is a principal customer of Texas Gas and became a party to this case because a decision in favor of Shell would have an adverse impact upon it and the ultimate consumers it serves.

> *"If at any time after December 31, 1951, Buyer shall enter into a contract providing for the purchase by it of gas* produced from a field or fields located, and delivered to Buyer, within a radius of fifty (50) miles of any point of delivery provided hereunder, Buyer shall forthwith notify Seller of such fact, *and if the price* per one thousand (1000) cubic feet *at any time payable under such other contract is higher* than the price payable hereunder, each price payable hereunder which is less than the price payable at the same time under such other contract shall be immediately increased so that it will equal the price payable under such other contract. In determining whether the price payable under such other contract is 'higher' than the price payable for gas under this contract, due consideration shall be given to the provisions of this contract as compared with such other contract as to quality of gas, delivery pressures, gathering and compressing arrangements, quantity, provisions regarding measurement of gas, including deviation from Boyle's Law, taxes payable on or in respect of gas delivered and all other pertinent factors." (R. 66-67, Sec. 3)*

B. The 1943 Atlantic Contract and the 1953 Price Redetermination

When Texas Gas entered into the Shell contract, it was a party to a gas purchase contract with Atlantic, which had been entered into in 1943.** This contract provides

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* Emphasis is supplied throughout this brief.

** It covers the North Tepetate Field, Acadia Parish, Louisiana (Item E, R. 81-96). It was originally entered into by Atlantic and Defense Plant Corporation as of September 1, 1943. Texas Gas purchased the pipeline operated by the Government and on May 11, 1949 became an assignee of the Government's rights and obligations under the gas purchase contract with Atlantic (Item H, R. 105). The 1943 Atlantic contract obligates Texas Gas to purchase up to a daily average of 25,000,000 cubic feet of gas for the producing life of the gas field, but not to exceed 25 years (R. 84, 90-91).

for a fixed price during the first five-year period, and, for the remaining four five-year terms, it stipulates that:

> "(b) At the end of the first five-year period, Buyer and Seller are to reach an agreement as to the price for gas sold and delivered under this contract during the second five-year period. The price to be paid during such second five-year period is to be agreed upon at the beginning of such period after a survey of prevailing prices for gas being sold in similar quantities in the southwestern part of Louisiana.
>
> "(c) During succeeding five-year periods, prices to be paid will be determined at the beginning of each period in the same manner as provided for in paragraph (b) above.
>
> "(d) In the event that the parties are unable to agree upon the price to be paid for gas after the first five-year period, in accordance with the arrangements set forth in paragraphs (b) and (c) above, such determination shall be submitted to arbitration in accordance with Condition XII" (Item E, R. 86).*

In accordance with this price redetermination provision, Texas Gas and Atlantic redetermined the price for the period beginning September 1, 1953, without need of arbitration, at 12.2¢, plus .3¢ severance tax and 1¢ gathering tax per Mcf (Exs. 5-7, R. 38-45). This price was recorded in a brief letter agreement dated February 17, 1954 (Ex. 9, R. 46-47).

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* Under Condition XII, each party selects an arbitrator, and a third arbitrator is chosen by the two arbitrators selected by the parties (R. 91-92). In the event that the two arbitrators fail to select a third arbitrator, he shall be appointed by the senior judge of the Fifth Federal Judicial Circuit. If one party should fail to designate an arbitrator, the sole arbitrator shall arbitrate the question alone.

C. Administrative Proceedings

The issue before the Commission was whether *price redetermination* in accordance with the terms and in performance of the 1943 contract for purchase of gas constituted post-1951 "enter[ing] into a contract providing for the purchase by [Texas Gas] of gas"—thereby establishing the initial qualification for increasing the price to be paid under the Shell rate schedule.

Although Shell knew of this action in March 1954 (R. 16), it raised no claim to a higher rate until it wrote to Texas Gas in October 1954 (Ex. 2, R. 35-36), after the Commission asserted regulation over independent producers in July (19 Fed. Reg. 4534-37).

On November 18, 1954 Shell tendered for filing with the Commission its contract with Texas Gas as the gas rate schedule. As required by regulation, Shell also submitted the May 1954 Texas Gas credit memorandum showing the price actually being paid (8.997¢ per Mcf) (Item D, R. 81). At the same time it offered a so-called "sample bill" which purported to show a 12.5¢ price, without explaining the basis for such price (Item C, R. 80). This was not a real bill or one ever sent to Texas Gas (R. 11-12).

On January 6, 1955, the Commission refused to accept the "sample bill", and stated that the rate schedule did not reveal any basis for charging a price different from the specified 8.997¢ rate (R. 151).

Shell remained silent for two years thereafter.* On

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* The record also contains evidence of other actions of Shell inconsistent with its claim to a higher rate, both before and even after it raised the issue and made its original tender for filing with the Commission. Briefly, they are: (1) between March and October 1954, and even as late as 1957, Shell accepted *monthly* credit statements from Texas Gas, each of which specifically stated and applied the untriggered 8.997¢ rate, and cashed *monthly* Texas Gas checks in payment of the credit statements (Ex. 11, R. 48-50); and (2) Shell made statements to the public accountants auditing the Texas Gas books, confirming as correct amounts due Shell which were calculated at the 8.997¢ rate (Ex. 12, R. 50-52, 53-57).

February 11, 1957 Shell proposed a further increase to 16.75¢ per Mcf, and took that occasion to explain to the Commission for the first time that it claimed that its June 7, 1954 rate should have been 12.5¢ per Mcf, rather than the 8.997¢ per Mcf it had been receiving and accepting, on the theory that a price increase has been "triggered" under its favored-nation clause by the Atlantic price redetermination (Item B, R. 74-75).* Thereupon, the Commission set a hearing to determine the rate "properly effective" as of June 7, 1954 (R. 110).

The Examiner issued an initial decision in favor of Shell (R. 112). Exceptions to that decision were filed by Commission staff counsel and by Texas Gas and Louisville. The full Commission unanimously reversed the Presiding Examiner's decision and determined that the favored-nation provision was not triggered by the Atlantic price determination (R. 126).** It denied Shell's application for rehearing (R. 143).

D. Proceedings in the Court of Appeals

On review, the Court of Appeals reversed the Commission's order, and denied petitions for rehearing filed by the Commission, Texas Gas and Louisville*** (R. 160-65, 166).

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* This filing for the further rate increase to 16.75¢ per Mcf is the subject of a separate proceeding pending before the Commission, and is not in issue here.

** The Commission also ruled, as an alternative ground, that the June 7, 1954 rate was the rate actually being charged and paid, i.e., 8.997¢ per Mcf. This ground was not pressed in the Court of Appeals and is not presented here.

*** The Court of Appeals remanded the proceeding to the Commission—not to reconsider the meaning of the "future contract" requirement—but to determine whether the *second requirement* for triggering was satisfied, namely, whether the Atlantic price was in fact "higher" when due consideration is given to various factors as required by the second sentence of the favored-nation clause (R. 165).

Summary of Argument

1. The lower court departed from the proper scope of its review in making its own independent assessment of "business practicalities" in the natural gas industry, its own de novo evaluation of industry practice and usage with respect to price provisions in rate schedules, and in substituting its own de novo interpretation of the meaning of the rate schedule for that of the Commission. As this Court has recognized, the proper scope of review by the appellate court is to ascertain whether the Commission's determination is reasonably supported. The reviewing court must affirm the Commission's determination where it has proper support.

Shell apparently would have it that this doctrine is inapplicable here because the interpretation of a rate schedule is a "matter of law" and not a subject of the Commission's special competence. Such an argument ignores the fact that the interpretation of a written instrument is essentially a factual determination.

The significance of terminology and the industry's understanding of, for example, "price redetermination" are, moreover, matters peculiarly within the special competence of the Commission. Indeed, interpretation of rate schedules is an integral part of the administrative and regulatory process delegated by Congress to the Commission.

Ad hoc judicial interpretation of rate schedules would be an invitation to chaos in the rate structure of the industry. It is only by the Commission's interpretation of rate schedules, based upon its continuing day-to-day experience with the needs and practices of the industry, that the Commission may achieve predictability and stability of rate

schedules and uniformity in accord with the mandate of the Natural Gas Act.

2. The essential distinction between "price redetermination" and "entering into a contract for the purchase of gas" within the meaning of the instant favored-nation clause is abundantly apparent from the explicit terms of the rate schedule itself. The Commission recognized and understood this distinction. Its understanding, based upon its knowledge of the natural gas industry and the use of terminology in rate schedules was confirmed by its reference specifically to provisions in other long-term contracts to which Shell was a party.

The "price redetermination" between Texas Gas and Atlantic was recognized by the Commission to be exactly that and nothing more. The parties were simply redetermining the price pursuant to the price term of an existing contract—a contract for the purchase of gas which had been entered into in 1943.

The validity of price changes pursuant to the terms of the existing contract and based upon an external standard or through arbitration is well accepted. The Commission's understanding that the Atlantic "price redetermination" was an act *pursuant to* the Atlantic contract and was not the *making of a new contract* for the purchase of gas is entirely in accord with precedent.

The Court of Appeals further committed error in adopting an interpretation of the instant price provision which

violates the explicit terms of the rate schedule itself and is without support in the record.

The instant favored-nation clause is expressly directed to a contract providing for the purchase of gas entered into by Texas Gas after 1951, and only to a higher price under such a future contract. The lower court, however, in interpreting this provision to carry out what it felt to be the "usual objective" of a favored-nation clause—to give Shell a "top price" for its gas—revised the explicit terms of the schedule to impose a new provision for price increases. Its findings, we submit, are without support and its rationale unsound.

Argument

Our brief is addressed to two propositions:

(1) The lower court departed from the lawful scope of its powers of administrative review by making its own de novo evaluation of industry practice and usage and its own findings of fact and by substituting its own de novo interpretation of this rate schedule price provision for that made by the Commission.

(2) The Commission's determination of the meaning of this price provision was entirely supported—both legally and factually—and it was error to reverse it. Moreover, the interpretation adopted by the lower court is contrary to the explicit terms of the rate schedule itself and contrary to the facts of record.

POINT I

In interpreting the rate schedule de novo and in making its own findings and evaluation of industry usage the court below departed from the proper scope of review

It is apparent from the opinion below that the court determined the meaning of the instant price provision on the basis of its own assessment of the "realities of the situation" and "business practicalities" and adopted its interpretation to carry out what it felt was the "usual objective" of a favored-nation clause (R. 163-64).

In the present case the Court of Appeals went well beyond permissible bounds of court review of an agency determination. It not only made its own final and binding determination without giving any weight to the Commission's determination, but it also affirmatively made findings of fact, a task which is exclusively that of the Commission.

Affirmative fact finding by a reviewing court (absent a statutory provision for a trial de novo) has been condemned repeatedly by the Court. Under statutes such as the Natural Gas Act where agency findings are conclusive if adequately supported, the role of fact-finding is one exclusively reserved or delegated to the Commission.

Even if the findings of the Court of Appeals were correct or supportable (which we shall show is not the case here), a reviewing court may not make its own findings. The principle of law was precisely summarized in *Florida* v. *United States*, 282 U. S. 194, 215 (1931):

> "In the absence of such findings, we are not called upon to examine the evidence in order to resolve opposing contentions as to what it shows or to spell out and state such conclusions of fact as it

> may permit. *The Commission is the fact-finding body and the Court examines the evidence not to make findings for the Commission but to ascertain whether its findings are properly supported.*"

See also, e.g., *FTC* v. *Algoma Lumber Co.*, 291 U. S. 67, 73 (1934); *Crolley* v. *Tatton*, 249 F. 2d 908, 911 (5th Cir. 1957), *cert. denied*, 356 U. S. 966.

As applied to the Natural Gas Act, the Court has pointed out that the reviewing court is not authorized "*to make findings and substitute them for those of the Commission.*" *Colorado-Wyoming Gas Co.* v. *FPC*, 324 U. S. 626, 634 (1945).

As the Court implicitly held in *United Gas Pipe Line Co.* v. *Memphis Light, Gas and Water Div.*, 358 U. S. 103, 114-15, the task of the reviewing court is to ascertain whether the Commission's interpretation of a rate schedule is properly supported. Thus, the Court concluded:

> "* * * we are satisfied that the Commission's determination as to the meaning of the service agreements here involved was amply supported both factually and legally."

See also *United States* v. *Interstate Commerce Commission*, 198 F. 2d 958 (D. C. Cir. 1952), *cert. denied*, 344 U. S. 893.

Shell apparently urges that the present issue is purely one of law (Brief in Opposition to certiorari, pages 14-26 and 26-28) and apparently would have it that the interpretation of a rate schedule is not a matter for the Commission's special competence.

While we are here concerned with finding the meaning of written language in a formal instrument and the result should be primarily predicated upon its express language, the interpretation of the meaning of a written provision and the significance of the inferences to be drawn from

terminology to arrive at meaning and purpose are essentially factual determinations. See Thayer, *A Preliminary Treatise on Evidence* 203-04, 206 (1898); 3 Williston, *Contracts* §616 (rev. ed. 1936); Stern, *Review of Findings of Administrators, Judges and Juries: A Comparative Analysis,* 58 Harv. L. Rev. 70, 111 (1944).

Moreover, the reasons why interpretation of contracts is sometimes characterized as a "matter of law" in the purely judicial system lend no support to the Shell position. The use of this label denotes an allocation of functions, within the judicial system, as between the judge and jury. This separation of powers apparently exists for two reasons of policy: (1) a presumed lack of sufficient experience on the part of the average juror, and (2) a desire to obtain some uniformity of decision from the fact that various judges will adhere to what they deem to be persuasive published precedents.*

But, in the administrative realm, the experience with the industry is found with the Commission, which also, as a single source of decision, will attain much greater uniformity of interpretation. Thus, to the extent that a distinction between "fact" and "law" is drawn in the administrative field, the way in which such a distinction is drawn, and its meaning and purpose, are very different than in the

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* *Cf.* Thayer, *A Preliminary Treatise on Evidence* 206 (1898); 3 Williston, *Contracts,* §616 (rev. ed. 1936). Also of modern significance is the procedure, invented by Lord Mansfield and others, of using special juries to obtain expert advice and reports on mercantile usages, which, when *reasonable*, were adopted as foundation stones in the building of interpretive precedents in commercial law. See Thayer, *op. cit. supra,* at 259. This early prototype of the modern administrative process is another reflection that, intrinsically, interpretation of commercial instruments has a factual basis, needs expert guidance and should be a vital part of administering a specialized industry, and that administrative interpretation should not be upset unless it is unreasonable.

purely judicial system. As the Court made clear in *Memphis* (358 U. S. 103) and in *Dobson* v. *Commissioner*, 320 U. S. 489, 499-500 and *United States* v. *Western Pacific R. R.*, 352 U. S. 59, 64-67, the distinction for purposes of administrative law is whether the issue calls for uniform and expert agency treatment.

The Court recently recognized the importance of uniformity in the agency's interpretation of railroad collective bargaining agreements and took judicial notice that their provisions were of a technical nature requiring a specialist to ascertain their meaning. *Pennsylvania R.R.* v. *Day*, 360 U. S. 548, 553. See also, *Slocum* v. *Delaware, L. & W. R.R.*, 339 U. S. 239, 243.

In interpreting rate schedules filed under the Natural Gas Act, the Commission is concerned with the meaning of the language expressly written into the instrument and this task is an integral part of the administrative process committed to the Commission by Congress. Moreover, administrative interpretation secures the twin benefits which the administrative process has to offer, namely, the familiarity of the Commission with the technical problems and practices of the industry being regulated and the uniformity and consistency of interpretation which come from the centralized agency.

Uniformity is obtained through the same provisions being interpreted the same way by the single agency. In an even broader way, overall consistency will emerge in time from a delineation of differences and subdifferences in various clauses, and from taking due account of the interrelationships among them. Of course, experience with the industry must go hand-in-hand with evolving such a body of administrative precedents, for only one who is knowl-

edgeable about the field is able to tell with assurance which clauses are essentially the same, where the differences lie and what the various interrelationships are among the several provisions. Only by such agency regulation may the stability and predictability of gas rate schedules be achieved.

Uniformity of interpretation is particularly desirable in the regulation of the natural gas industry. Although producer gas sales contracts are each individually negotiated with the purchasing pipeline, many contain provisions which are substantially identical. For example, as noted in our petition for certiorari (at p. 8), of the innumerable producer rate schedules containing favored-nation clauses, several hundred also contain a "future contract" limitation comparable to that here involved. In addition, such uniformity facilitates the Commission's discharge of its responsibility, under Section 4(b) of the Act, to eliminate undue discrimination "in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service."

The various elements discussed above were aptly summarized in the present proceeding by Commissioner Connole, when he said:

> "Preliminary resort to the Commission is required because the *inquiry is essentially one of fact and of discretion in technical matters; and uniformity in the interpretation of so common a clause as is involved here can be obtained only if its determination is left to the Commission.*" (R. 136)

Ad hoc judicial determination of a rate schedule as if it were nothing more than an unique contract between two private parties is an invitation to chaos in the rate structures

of natural gas companies. This must ultimately operate not only to the injury of the industry but to the ultimate economic injury of the consumer.

POINT II

The Commission's determination was fully supported and it was error to reverse it

In departing from the proper scope of review in this case, the lower court attributed a meaning and purpose to a provision in the Shell rate schedule which not only contradicts the clear intendment of the explicit terms of the schedule itself but is a substantive illustration of the practical wisdom of the rule against trial de novo in a reviewing court.

The instant favored-nation clause was expressly directed to contracts providing for the purchase of gas which Texas Gas might enter into after December 31, 1951.

This "future contract" requirement in the Shell contract was not some accidental or unintended combination of words. The clause was not directed to any higher price under any circumstances. Throughout the favored-nation provision reference is made only to the higher price under such other future contracts. Moreover, the fundamental distinction between "price redetermination" under an existing contract and "entering into a contract providing for the purchase of gas" is consistently reflected in the rate schedule itself.

The terms of the rate schedule

The Shell contract for the purchase of gas is a typical instrument covering acquisition of a large volume of gas over a long period. It necessarily contains detailed provi-

sions as to quality, pressure, billing and payment, warranty of title and other appropriate matters.

Provision is made for a fixed increase in price at given intervals throughout the life of the agreement (Article VI, Section 1, R. 65). In another section—a "price redetermination" clause—provision is made for Shell to obtain an increase in price in 1962 and again in 1967 by agreement between the parties (or arbitration) based upon the average of the three highest prices being paid by various buyers in Shell's area under comparable purchase arrangements (Section 4, R. 67-68).

The favored-nation section also provides for an increase:

> "If at any time after December 31, 1951 Buyer shall enter into a contract providing for the purchase by it of gas . . . and if the price . . . payable under such other contract is higher than the price payable hereunder . . ." (Section 3, R. 66-67).

In the Shell contract, when reference is made to "payment of prices" or an "agreement to pay a price", those words are used.

> "The prices to be paid by Buyer for gas" (Article VI, Section 1, R. 65).
>
> "Buyer agrees to pay in full the present gathering tax . . ." (Section 2, R. 65).

Similarly, when reference is made to price redetermination, those exact words are used:

> "Seller may request a price redetermination . . . Such determination is to be made by the parties or, if they are unable to agree, by the arbitrators" (Section 4, R. 67).

The word "redetermination" also appears in a provision for a redetermination of reserves during the life of the contract (Article II, Section 5, R. 63).

The expression, "enter into a contract for the purchase of gas", does not appear solely in the provision in dispute. This expression (or an equivalent)—entirely different from "price redetermination" and "agreement to pay"—appears elsewhere in the Texas Gas-Shell contract. The context, we submit, demonstrates conclusively the definite meaning and scope of the words "enter into a contract providing for the purchase of gas."

At the outset of this contract, it is provided (R. 57-58):

> "*This Contract*, made and *entered into* as of May 1, 1951 • • •"
>
> "WHEREAS, under date of October 1, 1943 Shell Oil Company, Inc., *entered into a contract for the sale of gas* • • •"
>
> "WHEREAS, • • • Buyer and Seller now desire to rescind said contract and *enter into a new contract for the purchase of gas* • • •"•

There can therefore be no doubt that the phrase "enter into a contract providing for the purchase of gas" means an instrument, such as the Shell contract, *really* "providing for the purchase of gas," by covering the important elements of quality, pressure, etc. The difference between "price redetermination" under an existing contract and

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• Further proof that the terms of the "future contract" limitation are used as a precise phrase of art and are not some accidental or unintended combination of words, appears within the terminology of the favored-nation clause itself (R. 66-67). The limitation, stated at the threshold of the clause, is woven throughout both sentences by consistent use of the phrase "such other contract", which operates to refer back to and incorporate the limitation. The fact that "contract for purchase of gas" does not mean a bare act of price redetermination, but rather denotes a full-scale contract for purchase containing *all* of the various detailed provisions necessary to the long-term relationship, is also shown by the second sentence of the clause. This sentence specifically refers to those various complex provisions, in requiring that due consideration be given to them in determining whether the price is "higher".

"entering into a contract for the purchase of gas" is thus quite apparent from the carefully drawn terms of the Shell contract itself.

It is in light of this careful and consistent usage of terminology—terms well known in the industry—that the price redetermination in 1954 by Texas Gas and Atlantic *pursuant to a pre-existing contract* must be viewed.

The Atlantic price redetermination

The Atlantic contract for the purchase of gas was "entered into" in 1943 (Item E, R. 81-96). Its price term provided for the payment of a fixed price for the first five years, plus tax reimbursement (R. 85). During succeeding five-year periods, the price to be paid was to be agreed upon "after a survey of prevailing prices for gas being sold in similar quantities in the southwestern part of Louisiana" (R. 86). Should the parties be unable to agree the price was to be determined by arbitration.

In 1953-54, pursuant to this price provision, the Texas Gas-Atlantic price was redetermined. A letter evidencing such redetermination was executed which recites that in 1943 the buyer "entered into a gas purchase contract" with Atlantic and that "In accordance with Paragraph III [the price provision] of said contract" it had been agreed that the price for the third five-year period shall be 12.2¢ plus tax reimbursement (Ex. 9, R. 46).

This act was of no different character than a price redetermination under the Texas Gas-Shell contract (see Item A, R. 67-68). Certainly it was not contemplated under the Shell contract that in 1962 and again in 1967 Texas Gas would enter into a contract for the purchase of gas with Shell. The parties would merely redetermine the price pursuant to the provisions of their existing contract which would continue in full force and effect.

A. The Commission's Determination Is Fully Supported

It was within its setting as part of a gas rate schedule that the "future contract" requirement of the favored-nation provision was considered by the Commission. As is apparent from the terms of the schedule itself, they reflect the interest of both the pipeline and the producer and the needs of a buyer and seller in the gas industry—facts known to the Commission. The significance and interrelation of the various parts of the price term of this schedule—including provisions for fixed increases, price redetermination, and favored-nation increases—must, of course, invoke the special competence of the Commission.

The understanding of the industry, including these contracting parties, of the difference between "price redetermination" under an existing contract as opposed to "entering into a contract for the purchase of gas" is clearly a matter which is the subject of the Commission's knowledge based upon the thousands of rate schedules filed with it under the Natural Gas Act and its day-to-day regulation of the industry.

The Commission found no difficulty in understanding the "future contract" limitation. Unanimously, the Commission found that the limitation required entry into a post-1951 contract for the purchase of gas before the Shell favored-nation clause is triggered and found that the Atlantic price redetermination was not such an act.

The technical accuracy of the Commission's interpretation was moreover confirmed by its reference specifically to various other of Shell's favored-nation provisions (R. 147). The Commission with an understanding of industry usage found a striking and revealing difference between the draftsmanship and pattern of (1) the clause with the "future contract" limitation, and (2) the type without that limitation (R. 147; Item J, R. 106-110).

As the Commission noted, the clear meaning of this "future contract" favored-nation clause and its significance—that it would be operative only as to future contracts for the purchase of gas and not in the event of a price redetermination under existing contracts as well—is demonstrated by the favored-nation clauses in such other long-term gas contracts to which Shell was a party and to which the Commission adverted. For example, in the Shell-Texas Eastern agreement, entered into in 1948, the favored-nation clause contains language in direct contrast with the language of the Shell contract here in dispute. That favored-nation clause provides for increase to any higher price paid under any *existing or future* contract. It begins:

> "If Buyer *has entered into or should hereafter enter into a contract* • • • *for the purchase of gas* • • •" (Item J, R. 107).

The favored-nation clause of the other Shell contracts of record similarly include favored-nation clauses under which a seller, such as Shell, can obtain as high a rate as that paid to any other seller as a result of price redetermination, escalation, or otherwise. Thus, in another long-term contract entered into by Shell in February 1951, the favored-nation clause provides:

> "If at any time the cost per MCF of gas purchased by buyer from any gas producer • • • shall be greater than the cost per MCF of gas purchased hereunder, buyer will increase the price per MCF payable to seller for gas delivered hereunder • • •". • (R. 106.)

• This broad provision also appears in the agreement between Tennessee Gas and Shell Oil and others of January 1950. The clause there provides:

> "If at any time after September 1, 1952 the cost per MCF of gas purchased by buyer • • • shall be greater than the cost per MCF of gas purchased hereunder, buyer will increase the price per MCF to seller for gas delivered hereunder" (R. 108).

See also the agreement between Natural Gas and Shell Oil of February 1950 and its favored-nation provision (R. 109).

There can be no stronger factual evidence of the parties' actual intent and understanding than the explicit terms of their agreement. Here, moreover, the Commission's determination was supported by the substantive evidence of Shell's contracting experience and was borne out by the obvious contrast of the instant provision with broader provisions for price increases which make no distinction between existing and future contracts. In all, over thirty contracts between Shell and other interstate pipeline purchasers of gas were before the Commission (Item J, R. 106).

This finding of the meaning is conclusive because there is not the slightest doubt that Atlantic and Texas Gas were redetermining price in performance of their underlying contract to purchase and were not entering into a new one. The terse 1954 letter recording the redetermined Atlantic price (Ex. 9, R. 46) establishes this, and also demolishes any thought that, as a "business practicality", the parties to the 1943 Atlantic contract were entering into a new contract for the purchase of gas.

The determination of the Commission, has, moreover, entire warrant in law. The process of interpretation, as we have indicated, is essentially a factual question. Accordingly, "the law" of any particular jurisdiction is seldom determinative of the contracting intent of the parties. See Goodrich, *Conflict of Laws,* Section 112, p. 338 ff. (3d ed. 1949).

In any event, the Commission's understanding that the Atlantic "price redetermination" was an act *pursuant to* the Atlantic contract and was not the *making of a new contract for the purchase of gas* is entirely in accord with precedent.

The validity of arbitration or appraisal clauses, as well as of objective price standards, is of course well

accepted.* Their use to make provision for price changes is common in the industry as is well known to the Commission.

As the Commission properly understood, the obligation to pay a price which has been changed in accordance with such a provision rests upon the original contract, of which the price term is an integral part. Thus, in *Phillips Petroleum Co.* v. *Federal Power Commission*, 227 F. 2d 470 (10th Cir. 1955), *cert. denied*, 350 U. S. 1005, the following was said about a price which was recorded:

> "But it was nonetheless in force and effect and was being paid *not by force of letter agreements, but by force of the binding effect of the escalator clauses which operated to fix the prescribed rate in accordance with the formula in the contract. The letter agreements were merely executory of the contract between the parties*" (227 F. 2d at 475).

Furthermore, the understanding of the Commission entirely comports with the Court's recent decision in the

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* At common law and under sales and arbitration acts, appraisal or arbitration clauses are enforced by the remedy of damages, if not by specific performance. See *e.g.*, *Red Cross Line* v. *Atlantic Fruit Co.*, 264 U. S. 109, 121; *Texas Co.* v. *Z. & M. Independent Oil Co.*, 156 F. 2d 862, 866-67 (2d Cir. 1946); 5 Williston, *Contracts* §1421, at 3967-68 (rev. ed. 1937); 6 Williston, *Contracts* §1921A (rev. ed. 1938); 1 Williston, *Sales* §176 (rev. ed. 1948). As to price standards, see, *e.g.*, *Cities Service Gas Producing Co.* v. *Federal Power Commission*, 233 F. 2d 726 (10th Cir. 1956), *cert. denied* 352 U. S. 911; *May Metropolitan Corp.* v. *May Oil Burner Corp.*, 290 N. Y. 260, 265, 49 N. E. 2d 13, 15-16 (1943); *Col-Tex Refining Co.* v. *Coffield & Guthrie, Inc.*, 196 F. 2d 788, 790-91 (5th Cir. 1952). The fact that there may be differences between the parties in applying a yardstick does not prevent the yardstick from being fully binding. See *Brassert* v. *Clark*, 162 F. 2d 967, 971-72 (2d Cir. 1947).

Memphis case (358 U. S. 103). There, the Court affirmed the Commission's determination that new rate schedules filed by the pipeline company did not change the contract with its customers, but merely changed the prices in accordance with the terms of the original service contract. The buyer was bound to pay the new prices because his original contract expressly provided that the price provision was variable and that he should pay the price as changed from time to time in accordance with the terms of the contract.

We submit that the determination of the Commission was amply supported and should have been affirmed.

The Court of Appeals should be reversed, we submit, on the ground that the Commission's determination was amply supported both factually and legally, as in the *Memphis* case (358 U. S. at 114).

B. The Lower Court's Interpretation is Without Factual or Legal Support and is Contradicted by the Record

The lower court's analysis of the record

To carry out what it felt to be the objective of the instant provision—to give Shell a "top price" for its gas—the lower court, of course, did not rely upon the terms of the schedule. Rather, it made certain findings.

The court's ultimate finding was that certain facts "tend strongly to demonstrate that the intention of the parties was for *any higher price*", to trigger a Shell price (with one possible exception) (R. 163).

To this end, the court first found that Texas Gas had desired a 20-year contract which "was for a term longer than Shell had at that time contracted for, at least in that area" and "[b]ecause of the difficulty in establishing a price

for so long a period the clause in question was agreed upon".

The fact of the matter is that even of the contracts now in this record, nine of them were executed by Shell prior to the Texas Gas contract. *Every one of these prior contracts has a stated term of 20 years or more.*•

Moreover, Shell did not exclusively rely upon the favored-nation clause for price increases over the term of the contract. Shell would obtain increases in fixed amounts at certain intervals throughout the contract (Article VI, Section 1, R. 65). Shell could obtain price redetermination in 1962 and again in 1967 if the prevailing prices in its area for comparable arrangements—no matter who the buyer and, no matter how such prices were arrived at—were higher than Shell's then contract price (Section 4, R. 67-68).

The court then apparently reasoned that "any higher price" paid by Texas Gas was intended to trigger a rise in the Shell contract since "at the time of contracting Shell knew (Texas Gas) was purchasing gas from Atlantic but was not familiar with the specific terms of the contract" (R. 163). But, the fact is—which the lower court does not dispute—that at the time of contracting Shell knew that sales were being made by Atlantic *under an existing contract*. It knew that that contract for the purchase of gas from Atlantic had already been entered into.

• The other Shell contracts are not set out in full in the printed Transcript of Record and the excerpts and summary do not cover the provisions for how long they are in effect (Item J, R. 106-10). However, four of the prior, long-term contracts referred to in the text above are those excerpted in the printed record (Shell Rate Schedule Nos. 6, 10, 12 and 18). Of course, these do not represent all of Shell's long-term contracts executed prior to the present one. As the Commission is well aware, contracts for terms of twenty years or more are prevalent throughout the industry (by mid-1956, well over 2,000 rate schedules were in this category (Exhibit 2LC, FPC Docket No. 9277, *et al.*, the so-called "Omnibus Case")).

We submit that knowing there was an existing contract with at least one other seller in this area, when Shell entered into its contract with Texas Gas in May 1951, Shell was entirely alert to the limitation of a favored-nation clause which began:

> "If at any time after December 31, 1951, Buyer shall enter into a contract providing for the purchase by it of gas. . . ".

Thus, the court's analysis of the record is neither supported by the record nor can it support an interpretation which violates the explicit terms of the rate schedule itself.

The court apparently gave no weight to the determination of the Commission made in the light of its undoubted knowledge of the significance of "price redetermination" as opposed to "entering into a contract for the purchase of gas." Moreover, the court apparently gave no weight to the explicit difference between the instant favored-nation clause and those contemplating an increase in price in the event a higher price is paid by the buyer whether or not the increase occurred under an existing or a future contract.

To be compared with the court's assessment of "business practicalities" is the Commission's knowledge of the "practicalities" of the gas industry and the economic significance and impact on existing rate structures of a new price paid for the acquisition of gas. The Commission recognized the obvious and important purpose of the limitation of this favored-nation clause, as in others like it, to future contracts for the purchase of gas.

Thus, under this clause, the triggering of an increased rate to a chain of purchasers is restricted, among other things, to an event over which the pipeline has a measure of control—an event which is to be distinguished from obligatory price increases under fixed-price escalation or "pre-

vailing price" provisions in pre-existing contracts for purchase.

The economic significance to the pipeline of such a limitation is in the right and freedom to weigh the impact of a higher price for the acquisition of gas upon existing rate structures, in choosing whether, when and where to acquire new gas, and at what price.

The economic significance to Shell of this limitation is that if Texas Gas should enter into a contract for the purchase of new gas at a price higher than the Shell price, Shell would then obtain an increase under its favored-nation clause. On the other hand, the prevailing market price, as such, would be obtained by Shell—not under the favored-nation clause—but under its own price redetermination clause which would become operative on the dates specified.

The court further apparently ignored the substantive evidence of the conduct of the parties which was entirely consistent with their understanding of the difference between price redetermination and "entering into a contract for the purchase of gas"—also an industry understanding the Commission's knowledge of which was not disputed.

Thus although Shell learned about the Atlantic price redetermination in March, 1954 (R. 16), it did not notify Texas Gas that it thought its price had been "triggered" until more than six months later in October, 1954 (Ex. 2, R. 35). In its original submission to the Commission in November, 1954, Shell tendered its contract and the actual May, 1954, credit memorandum showing the unescalated rate, together with a "sample" billing at the higher rate (Item C, R. 80). When the Commission requested an explanation (R. 151), Shell waited more than two years before presenting to the Commission its justification for the higher rate (Item B, R. 72-77).

During this same period, from March, 1954, to February, 1957, the credit memoranda submitted by Texas Gas and its checks in payment for the gas under the Shell contract uniformly were based upon the unescalated price provided by that contract (Ex. 11, R. 48-50). In accepting those checks over this extended period, Shell never attempted to preserve any claim to the higher price. Moreover, in six of seven statements made by Shell during this period to public accountants who were auditing the books of Texas Gas and its predecessor, Shell stated that balances due to it as shown by such books, which were calculated on the basis of the unescalated price, were correct (Ex. 12, R. 51-57).

We submit that the decision of the court below can not be based either upon any analysis of the record or the terms of the rate schedule.

On the contrary, if any further evidence were needed of the meaning of the favored-nation clause beyond the explicit terms of the clause itself and the schedule of which it is a part, the evidence of the contract usage of Shell itself and the evidence of the conduct of the parties—all evidence of record—reaffirm that the terms of this provision mean exactly what they say. They will not admit of the interpretation adopted by the court below.

The lower court's rationale is unsound

The lower court also erred, even if, in determining the intention of the parties, it reasoned from what it found to be the legal significance of price redetermination under the Atlantic contract. Its rationale, we submit, is unsound.

Performance of the original contract with Atlantic did not require the parties to enter into subsequent contracts, as the lower court reasoned, but required the parties to perform in accordance with the price term. Their obliga-

tions rested upon the continuing existence of the original 1943 contract.

When, at each fifth anniversary of that contract, Texas Gas and Atlantic redetermined a different price to apply for the subsequent five years, they were not making a wholly new "contract for the purchase of gas". They were mutually determining a change in price, in accordance with an express provision of their original, and still fully operative, contract. A failure to agree on a precise price would not have frustrated the contract nor would it have been a breach of contract; but it would have at once brought into operation the apparatus for arbitration.

This provision is valid and binding on both parties and neither party had the right or the power to impede its inexorable operation. And, if the precise price for any period were determined by the operation of the arbitration clause, it would be as fully effective under the basic contract as if that price had been originally agreed to by the parties.

No one can doubt that Texas Gas would be bound to pay the price determined by arbitration; and its obligation in this respect derives from the original contract and not from any new or subsequent or succeeding contract. A new price fixed by an arbitrator would certainly not be one fixed by a new contract. The same is true of a new price fixed by redetermination as provided in the original contract.

As this court recognized in the recent *Memphis* case, the buyer is bound to pay the new and changed price because his original contract expressly provides that he should.

The novel view adopted by the court below was apparently developed on the basis of that court's special conception of "business practicalities" and "the realities of the situation." The lack of support for such findings demonstrates the wisdom of the rule that reviewing courts

may not interfere with the functions delegated to the administrative agencies and should accept the agency's determination unless it is unsubstantiated.

There is, we submit, no warrant in fact or law for the lower court's reversal of the Commission's determination.

Conclusion

To avoid duplication, we have not repeated in detail all the points made in the brief for the Commission, in which we fully join.

For the reasons stated in both briefs, the decision and judgment of the Court of Appeals should be reversed and vacated, and the order of the Commission should be affirmed.

Respectfully submitted,

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March 4, 1960.

APPENDIX A

Section 19(b) of the Natural Gas Act

[Rehearings: court review of orders]

(b) Any party to a proceeding under this chapter aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be transmitted by the clerk of the court to any member of the Commission and thereupon the Commission shall file with the court the record upon which the order complained of was entered, as provided in section 2112 of Title 28. Upon the filing of such petition such court shall have jurisdiction which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The

Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 346 and 347 of Title 28. [*]

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[*] Sections 346 and 347 of Title 28, referred to in subsec. (b), were repealed by act June 25, 1948, ch. 646, § 39, 62 Stat. 992, eff. Sept. 1, 1948, and are now covered by section 1254 of Title 28, Judiciary and Judicial Procedure.

APPENDIX B

Section 10(e) of the Administrative Procedure Act

[Judicial Review of Agency Action]

[SEC. 10. Except so far as (1) statutes preclude judicial review or (2) agency action is by law committed to agency discretion—]

(e) *Scope of Review.*

So far as necessary to decision and where presented the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of any agency action. It shall (A) compel agency action unlawfully withheld or unreasonably delayed; and (B) hold unlawful and set aside agency action, findings, and conclusions found to be (1) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law; (2) contrary to constitutional right, power, privilege, or immunity; (3) in excess of statutory jurisdiction, authority or limitations, or short of statutory right; (4) without observance of procedure required by law; (5) unsupported by substantial evidence in any case subject to the requirements of sections 1006 and 1007 [*] of this title or otherwise reviewed on the record of an agency hearing provided by statute; or (6) unwarranted by the facts to the extent that the facts are subject to trial de novo by the reviewing court. In making the foregoing determinations the court shall review the whole record or such portions thereof as may be cited by any party, and due account shall be taken of the rule of prejudicial error.

[*] Sections 7 and 8 of the Administrative Procedure Act.

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No. 716

In the Supreme Court of the United States

October Term, 1958

FEDERAL POWER COMMISSION, Appellant

v.

SHELL OIL COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE FEDERAL POWER COMMISSION

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In the Supreme Court of the United States

OCTOBER TERM, 1959

No. 170

FEDERAL POWER COMMISSION, PETITIONER

v.

SHELL OIL COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE FEDERAL POWER COMMISSION

OPINIONS BELOW

The opinion of the court of appeals (R. 160–165) is reported at 263 F. 2d 223. The opinions and orders of the Federal Power Commission (R. 126–137, 143–150) are reported at 18 F.P.C. 617 and 19 F.P.C. 74.

JURISDICTION

The judgment of the court of appeals was entered on January 27, 1959 (R. 165–166). A timely petition for rehearing was denied on March 4, 1959 (R. 166). By order of Mr. Justice Brennan, dated May 25, 1959, the time within which to file a petition for a writ of certiorari was extended to and including July 2, 1959. The petition for a writ of certiorari was filed on July 1, 1959, and was granted on October 12, 1959 (R. 169).

361 U.S. 811. The jurisdiction of this Court rests upon 28 U.S.C. 1254(1) and § 19(b) of the Natural Gas Act, 15 U.S.C. 717r(b).

QUESTIONS PRESENTED

The "favored-nation" clause of a contract for the sale of natural gas provided that the producer would be entitled to a price increase should the pipeline thereafter "enter into a contract providing for the purchase by it of gas" at a higher price. The pipeline thereafter agreed to a higher price under a pre-existing long-term contract with another producer which required that the price be redetermind every five years on the basis of the then-prevailing prices, the price to be fixed by arbitration should the parties fail to agree. In proceedings under the Natural Gas Act to determine respondent's effective rate, its contract having been filed as a rate schedule, the Federal Power Commission held that the price redetermination under the pipeline's prior contract with the other producer was not a new contract for the purchase of gas within the meaning of respondent's "favored-nation" clause and that respondent was not entitled to a price increase. The questions presented are:

1. Whether a court of appeals, on review of the order, may decide for itself the meaning of the "favored-nation" clause of respondent's contract or must accept the Commission's interpretation, if reasonably supported.

2. Whether the "favored-nation" clause of respondent's contract provided for a price increase in these circumstances.

STATUTE INVOLVED

Pertinent provisions of the Natural Gas Act (52 Stat. 821, 15 U.S.C. 717, *et seq.*) are set forth in the Appendix, *infra,* p. 52 *et seq.*

STATEMENT

1. Shell Oil Company ("Shell"), an independent producer of natural gas, sells gas produced in Southern Louisiana to the Texas Gas Transmission Corporation ("Texas Gas") under a 20-year contract (the "Shell contract") executed in 1951 (R. 57–71).[1] After the decision in *Phillips Petroleum Co.* v. *Wisconsin,* 347 U.S. 672, holding sales of natural gas in interstate commerce by independent producers to be subject to the Natural Gas Act (52 Stat. 821, 15 U.S.C. 717, *et seq.*), the Federal Power Commission directed such producers to file rate schedules showing their rates in effect on June 7, 1954, the date of that decision (18 C.F.R. 154.91, *et seq.*). In November 1954, Shell duly filed, as its rate schedule, its contract with Texas Gas, together with, as required, a statement showing the rate actually being received on that date, which was 8.997 cents per Mcf (R. 110, 127). Shell also filed, however, a "sample" billing statement purporting to show that the correct rate was 12.5 cents (*ibid.*; R. 80). The Commission, in January 1955, notified Shell that it would not accept the filing until an explanation of the effective rate was provided (R. 151). Shell took no action until February 1957, when, in filing a prospective rate change for the sale to 16.75 cents, it

[1] The contract was originally with Texas Gas' wholly-owned subsidiary, Louisiana Natural Gas Corporation. The corporations merged in June 1955 (R. 127).

aimed that its effective rate on June 7, 1954, was 2.5 cents by virtue of a price increase to which it had ecome entitled in 1953 under the "favored-nation" ause of its contract with Texas Gas (R. 72–77, 127).

The Commission suspended the proposed 16.75-cent ate pending a determination of its reasonableness[2] nd directed a hearing to determine the rate in effect n June 7, 1954 (R. 110–111, 127–128). After hearngs, the Commission determined that the effective ate in 1954 was 8.997 cents and directed that a revised illing statement so showing be filed with the contract s the rate in effect on June 7, 1954 (R. 134–135).[3] The court of appeals set aside the order, and reanded the case to the Commission (R. 160–165).

2. Admittedly, the rate in effect under the contract rior to 1953 was 8.997 cents, and the sole question efore the Commission was whether Shell had become ntitled to an increase under its "favored-nation" lause in 1953. The facts relevant to that issue are as ollows:

The "favored-nation" clause of the 1951 Shell contract provided (R. 66–67):

> 3. If at any time after December 31, 1951, Buyer [Texas Gas] shall enter into a contract

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[2] That proceeding is still pending before the Commission. The new rate (based upon another purchase of gas by Texas Gas admittedly within the favored-nation clause) went into effect after the expiration of the five-month suspension period, subject to the Commission's power to order refunds if the increased rate is ultimately found to have been unjustified. See 4(e) of the Act, 15 U.S.C. 717c(e).

[3] The contract itself had been accepted for filing in the order directing the hearing, with only the filing of the required billng statement being held in abeyance (R. 111).

> providing for the purchase by it of gas produced from a field or fields located, and delivered to Buyer, within a radius of fifty (50) miles of any point of delivery provided hereunder, Buyer shall forthwith notify Seller [Shell] of such fact, and if the price per one thousand (1,000) cubic feet at any time payable under such other contract is higher than the price payable hereunder, each price payable hereunder which is less than the price payable at the same time under such other contract shall be immediately increased so that it will equal the price payable under such other contract. * * *

At the time the Shell contract was made, Texas Gas was also buying gas in the same area from The Atlantic Refining Company under a long term contract (the "Atlantic contract") which had been executed on September 1, 1943 (R. 81–94).[4] The term of the contract was for the duration of the field from which the gas was supplied, but not more than 25 years (R. 90–91). The contract fixed the rate to be paid during the first five years and provided (R. 86):

> (b) At the end of the first five-year period, Buyer and Seller are to reach an agreement as to the price for gas sold and delivered under this contract during the second five-year period. The price to be paid during such second five-year period is to be agreed upon at the beginning of such period after a survey of prevailing prices for gas being sold in simi-

[4] The contract had initially been between Atlantic and the Defense Plant Corporation, but Texas Gas (through its subsequently-merged subsidiary) had acquired all the latter's rights on May 11, 1949 (R. 81, 105, 118).

lar quantities in the southwestern part of Louisiana.

(c) During succeeding five-year periods, prices to be paid will be determined at the beginning of each period in the same manner as provided for in paragraph (b) above.

(d) In the event that the parties are unable to agree upon the price to be paid for gas after the first five-year period, in accordance with the arrangements set forth in paragraphs (b) and (c) above, such determination shall be submitted to arbitration in accordance with Condition XII.[5]

Both the 1948 and the 1953 price redeterminations under that provision were agreed upon without resort to arbitration, the price fixed for the period beginning September 1, 1953, being 12.5 cents per Mcf.[6]

Shell contended that by agreeing to the 1953 price redetermination under the Atlantic contract Texas Gas had, after 1951, "enter[ed] into a contract providing for the purchase by it of gas" within the meaning of the Shell contract. Accordingly, it claimed to be entitled to an increase of its rates to the same level under the "favored-nation" clause of its contract.

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[5] Condition XII (R. 91–92) was a typical arbitration provision calling for the appointment by each party of one arbitrator and the selection of a third by the two so appointed or, if they failed to agree, by a designated judge. If either party failed to appoint an arbitrator, the other party's appointee was to be sole arbitrator. The decision of the arbitrators was to be "final and conclusive."

[6] R. 46, 96–97, 99–103, 119, 130–131, 132. The second price redetermination was not actually agreed upon until February 17, 1954, but, since it became effective in 1953, will be referred to as the 1953 redetermination. The 12.5 cents figure included .3 cent severance tax (R. 130).

3. Noting that the provision for arbitration made the price-redetermination provisions of the Atlantic contract definite and enforceable, the Commission, reversing its examiner (R. 112–126, 129), held that the 1953 redetermination agreement was but action which Texas Gas was obligated to take under its pre-existing contract with Atlantic and was not the entering of a new contract for the purchase of gas within the meaning of the Shell "favored-nation" clause (R. 129, 130–134).[7] In support of that interpretation of the Shell contract, the Commission, in its order denying rehearing, noted the numerous examples in the record of other contracts—to which Shell itself was a party—containing "favored-nation" clauses which, in contrast to the clause used here, were not limited in operation to higher prices paid under new contracts but were by their express terms equally applicable to price increases given under pre-existing contracts (R. 147).

4. The court of appeals vacated the Commission's order and remanded the case to the Commission, holding that the 1953 Atlantic price redetermination constituted the entering into of a contract for the purchase of gas under the Shell "favored-nation" clause (R. 160–165).[8] Although assuming for pur-

[7] As an alternative ground, the Commission also held that the price which Shell was actually receiving on June 7, 1954, was its effective rate as of that date (R. 129). That ground was abandoned in the court below in light of the court's intervening contrary decision in *Natural Gas Pipeline Co.* v. *Federal Power Commission*, 253 F. 2d 3 (C.A. 3), certiorari denied, 357 U.S. 927.

[8] The remand was to determine the precise amount, if any, by which the Atlantic redetermined price exceeded the Shell rate,

poses of decision that the Atlantic contract was enforceable and thus a "binding agreement-to-agree on the price for gas in each of the contract's last four five year periods" (R. 164–165), the court held (R. 164):

> * * * the fact cannot be avoided that, at least for purposes of the favored nation clause, the "entering of a contract for the purchase of gas" has not been accomplished until the price has been established. True, Atlantic was obligated to deliver gas for twenty years from 1943 but, just as important, Louisiana was bound to pay for it. And while there may have been enforceable means for settling the rate of payment in the event the parties could not agree, it would nonetheless be true that it was when the price was finally established, by whatever means, that a contract had thereupon been entered. Actually, if the Louisiana-Atlantic agreement of February 17, 1954, was not an entering of a contract we are at a loss as to how it would be properly and legally characterized. The situation fits best into the rubric of an accord itself taken as satisfaction. See 6 Williston on Contracts, §§ 1841, 1846 (rev. ed. 1938). Both parties gave up their rights under the original contract to proceed to arbitration, promising on the one side to pay and on the other side to accept the price reached.

The court further stated (R. 163) that the "usual objective" of a "favored-nation" clause "is to assure the seller a top price for its gas"; and that facts surrounding the negotiation of the Shell contract "tend

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taking into account the comparability of the terms and conditions of the sales (R. 165).

strongly to demonstrate that the intention of the parties was for any higher price paid by Louisiana to another producer to trigger a rise on the Shell contract to the same figure except possibly where a pre-existing contract already provided for a settled step-up in price."

SUMMARY OF ARGUMENT

The "favored-nation" clause in a 1951 contract for the sale of natural gas by Shell, an independent producer, to Texas Gas, a pipeline—which contract Shell filed with the Federal Power Commission as its rate schedule—provides for an increase in the price thereunder if the buyer should thereafter "enter into a contract providing for the purchase by it of gas" at a higher price. The substantive issue is whether this clause was triggered in 1953, when Texas Gas agreed to a higher price under a pre-existing long-term contract with another producer (the "Atlantic contract") which required the price thereunder to be redetermined every five years, the price to be fixed by arbitration should the parties fail to agree. The Commission held that it was not; it ruled that the "favored-nation" clause was triggered only if Texas Gas thereafter entered into a new contract for the purchase of gas, and that the 1953 Atlantic price redetermination "does not constitute [such] a new contract * * * but merely represents action taken under a pre-existing contract between Texas Gas and Atlantic" (R. 130; see R. 132). The court of appeals, interpreting the "favored-nation" clause *de novo* in the light of its own views as to the "usual objective" of such clauses, the reasons for including the clause in the Shell agreement, and the

"business practicalities" of the agreement (R. 163–164), set aside the Commission's interpretation.

I

Judicial review of the Commission's interpretation of a natural gas supply contract filed as a rate schedule is limited to a determination whether it is reasonably supported.

A. As a result of the Commission's extensive regulatory experience in the natural gas industry, it has acquired an insight into the industry's economics and business practices which is not shared by courts nor within their conventional experience. Consequently, the Commission is far better equipped than the courts to interpret natural gas purchase contracts which, in the case of independent producers such as Shell, constitute the rate schedules required to be filed with the Commission. In these circumstances, the Commission's interpretation of the rate schedule should be accepted by the reviewing court as long as it has "'warrant in the record' and a 'reasonable basis in law'" (*Unemployment Compensation Commission* v. *Aragon*, 329 U.S. 143, 153–154). Such limited judicial review not only places primary responsibility for decision in the expert body which "by specialization, by insight gained through experience, and by more flexible procedure" (*Far East Conference* v. *United States*, 342 U.S. 570, 575) is best qualified to decide these questions, but also achieves a uniformity of interpretation that is necessary for the effective functioning of the regulatory process.

B. Pertinent decisions of this Court support the limited scope of judicial review of the Commission's

interpretation of the Shell "favored-nation" clause here urged. In *United Gas Pipe Line Co.* v. *Memphis Light, Gas and Water Division,* 358 U.S. 103, 114, the Commission's construction of a natural gas purchase contract was described as involving "matters peculiarly within the area of the Commission's special competence," and was sustained since it was "amply supported both factually and legally." See also, *United States* v. *Western Pacific R. Co.,* 352 U.S. 59, 66–67, where the Court held that certain questions of tariff interpretation lay within the primary jurisdiction of the Interstate Commerce Commission because the decision thereof "involves an intimate knowledge of" the reasons why particular items received certain classifications—a knowledge which "is possessed not by the courts but by the agency * * *."

The fact, upon which respondent relies, that in other contexts questions of contract interpretation are characterized as "questions of law" for the court does not justify the reviewing court in construing the rate schedule *de novo.* For, as this Court has recognized, the distinction between "questions of fact" and "questions of law" is not the appropriate touchstone for determining the scope of judicial review of agency action. Rather, the scope of such review must depend upon a realistic analysis of whether the issue decided by the agency is so within its expertise as to make inappropriate the substitution of the reviewing court's judgment for that of the agency.

II

The Commission's conclusion that the Shell "favored-nation" clause was not triggered by the

Atlantic price redetermination was reasonable. It reflects, and rests upon, the significant distinction in the natural gas industry between "favored-nation" clauses that are triggered whenever a buyer pays a higher price and those that are triggered only when such higher price is the result of a new contract for the purchase of gas. The Shell clause clearly is of the latter kind.

A. In the negotiation of gas supply contracts, the distinction between "future contract" "favored-nation" clauses and those that are activated whenever the buyer pays a higher price for gas rests upon critical differences in the economic effect of the two kinds of clauses. Under the former clause, the pipeline retains some measure of control over increases in the cost of its existing gas supply, and over the timing of such increases. Under the latter, however, the pipeline has no control over such factors. Thus, to whatever extent a pipeline can limit the "favored-nation" clause in the contract currently being negotiated, there is a corresponding limitation upon price increases under that contract. For this reason, the scope of "favored-nation" clauses is the subject of keen bargaining between producers and pipelines.

The Commission correctly ruled that the Shell "favored-nation" clause here involved, which provides for escalation only if the buyer thereafter enters into a contract for the purchase of gas, was not triggered by a price redetermination under an existing contract. As the Commission pointed out (R. 147), other Shell sales contracts on file with the Commission used specific language when it was "intend[ed] that escala-

tions take place when prices were raised under either old or new contracts"—phrases such as "If at any time the cost" increases or "If Buyer has entered into or should hereafter enter into a contract" for the purchase of gas at a higher price (R. 106, 107, 147). In view of the obvious care with which the lengthy and detailed provisions of the Shell contract were drafted, it is reasonable to suppose that if the parties had intended the price to escalate whenever the buyer paid a higher price under an existing contract, they would have selected the language that Shell customarily employed to achieve that result. Instead, they used language that in terms provides for a price increase only if the buyer thereafter enters into a new gas supply contract. The Atlantic price redetermination did not constitute such a subsequent entering into of a new gas contract.

B. This Court has pointed out that "The primary aim of this legislation was to protect consumers against exploitation at the hands of natural gas companies" (*Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591, 610). The necessary effect of "favored-nation" clauses is to increase the price of natural gas in the field, and hence its price to the ultimate consumer. The Commission's construction of the Shell clause, which limits its operation to situations where the buyer enters into a new supply contract, thus furthers the consumer interest which the Act is designed to protect.

III

A. Even if the Shell rate schedule were open to *de novo* judicial examination, the court of appeals erred in holding that the Shell price was escalated

by the 1953 Atlantic price redetermination. The considerations, previously noted, that show the reasonableness of the Commission's interpretation of the Shell "favored-nation" clause also support that interpretation as an independent question of law.

B. The court of appeals treated the issue as turning on the legal characterization of the Atlantic price redetermination, *i.e.*, was the latter itself a "contract * * * for the purchase * * * of gas"? But the proper inquiry is not how the Atlantic redetermination might be characterized in some other context, but whether the parties to the Shell contract intended its "favored-nation" clause to apply to price redeterminations covering gas furnished under pre-existing supply contracts. The parties to the Shell contract did not so intend.

In any event, we submit that the court of appeals erred in holding that, even as a matter of contract law, the Atlantic price redetermination itself constituted a separate "contract * * * for the purchase * * * of gas." The Atlantic contract created a long-term commitment for the purchase of gas which remained in effect whether or not the parties were able to agree upon a new price at periodic intervals; if they were unable to do so, the price was to be fixed by arbitration. The 1953 price redetermination was not a new gas purchase contract, but rather a step taken in performance of the 1943 contract in accordance with the specific provisions for periodic price adjustments. The single-page letter in which the 1953 price readjustment is set forth does not contain the numerous detailed provisions normally found in gas purchase

contracts. Moreover, it recognizes the continuing validity of the 1943 contract, since it recites that the price change is being made "in accordance with Paragraph III of said contract" (R. 46).

ARGUMENT

The substantive issue in this case is the meaning of a "favored-nation" clause in a natural gas purchase contract that was filed with the Federal Power Commission as a rate schedule. The Commission, in the exercise of its regulatory functions under the Natural Gas Act and applying its expertise in the highly specialized and technical natural gas business, construed the clause as not authorizing a higher rate in the circumstances here involved. The court of appeals, interpreting the clause *de novo* in the light of its own views of the "usual objective" of such clauses, the reasons for including the clause in the Shell contract, and the "business practicalities" of the agreement, reached the contrary conclusion.

We shall show, however, that the proper scope of judicial review of the Commission's construction of such a contract is far narrower: The court itself cannot determine *de novo* the meaning of the "favored-nation" clause, but must accept the Commission's interpretation if reasonably supported. That conclusion, we believe, follows from the basic character of the Commission's action in construing the contract—*i.e.*, the application of its expert knowledge and judgment to a highly technical field—and from settled principles governing the relationship between courts and agencies when the former are called upon to review the exercise of the latter's expert judgment. We shall fur-

Commission's construction of the on" clause here involved was a ıe, based upon the industry custom egotiating such clauses.' Finally, even if the meaning of the clause o examination by the court of aped in holding that the price redehe Atlantic contract triggered the ause of the Shell contract.

I

THE COMMISSION'S INTERPRETATION ED AS A RATE SCHEDULE IS LIMITED ›N WHETHER IT IS REASONABLY SUP-

›N'S CONSTRUCTION OF THE "FAVORED-NAD UPON THE AGENCY'S EXPERTISE IN THE ATURAL GAS BUSINESS, SUCH INTERPRETANLY LIMITED JUDICIAL REVIEW

rst enacted the Natural Gas Act l), the Federal Power Commission

rther erred by making its own findings ıntering into such a contract. See, *e.g.*, ı *Co.* v. *Federal Power Commission*, 324 *Trade Commission* v. *Algoma Lumber* f the court considered the Commission's dequately supported by the language of factors relied on by the Commission, d have been to remand the case to the r findings. See, *e.g.*, *Securities & Ex-Chenery Co.*, 332 U.S. 194, 196; *Federal ission* v. *Pottsville Broadcasting Co.*, 309 e appropriateness of here applying this the showing, *infra*, pp. 31–36, that the in accord with the business practicalities

has been charged with the regulation of companies engaged in transporting, or selling for resale, natural gas in interstate commerce. In the course of this regulation, and particularly since this Court's decision in *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672, in 1954, the Commission has been dealing daily with the needs and problems of all segments of the natural gas industry, including producers.[10] More than 10,000 basic contracts of independent producers have already been filed with the Commission.[11] As a result of this extensive regulatory experience, the Commission has acquired an insight into the economics and business practices of the industry which is not shared by the courts nor within their conventional experience. Consequently, the Commission is far better equipped than the courts to interpret and evaluate the natural gas purchase contracts which are not only essential to the business but which, in the case of independent producers, themselves constitute the rate schedules required to be filed with the Commission.[12]

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[10] This Court has recognized the Commission's expertise in matters relating to the natural gas industry. *United Gas Pipe Line Co.* v. *Memphis Light, Gas and Water Division*, 358 U.S. 103, 114; *Federal Power Commission* v. *Colorado Interstate Gas Co.*, 348 U.S. 492, 501; cf. *Interstate Power Co.* v. *Federal Power Commission*, 236 F. 2d 372, 385 (C.A. 8), certiorari denied, 352 U.S. 967.

[11] The Commission has not as yet required the independent producers, as it has the pipeline companies, to convert their gas sales contracts to the tariff-and-service agreement method of fixing rates. See *United Gas Pipe Line Co.* v. *Memphis Light, Gas and Water Division*, 358 U.S. 103. Consequently, the producers are still selling gas under separate contracts with each purchaser.

[12] The Commission's regulations under the Natural Gas Act provide that the "rate schedules" required to be filed by inde-

Accordingly, when, as here, questions as to the interpretation of such rate schedules arise in Commission proceedings, it is not only appropriate, but necessary, in order to attain "the objects of the act * * * without constant and disconcerting friction," that the Commission's interpretations should control unless plainly erroneous. Cf. *Securities & Exchange Commission* v. *Associated Gas & Electric Co.*, 99 F. 2d 795, 798 (C.A. 2). In order to affirm the Commission, therefore, the reviewing court need not find that "[the administrative] construction is the only reasonable one, or even that it is the result * * * [the court] would have reached had the question arisen in the first instance in judicial proceedings. * * * All that is needed to support the Commission's interpretation is that it has 'warrant in the record' and a 'reasonable basis in law'" (*Unemployment Compensation Commission* v. *Aragon*, 329 U.S. 143, 153–154).

Sound considerations of public policy justify such a limitation upon review of the Commission's interpretation of natural gas contracts. Primary responsibility for the resolution of these issues is thereby placed upon the body which "by specialization, by insight gained through experience, and by more flexible procedure" (*Far East Conference* v. *United States*,

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pendent producers are "the basic contract and all supplements or agreements amendatory thereof," pursuant to which the producers sell gas to the pipelines. 18 C.F.R. 154.92–154.94. Changes in such rates cannot be made unless first filed with the Commission pursuant to Section 4(d) of the Act (18 C.F.R. 154.94 (a)); a rate change resulting from the operation of a price readjustment provision in an existing contract constitutes a "change in rate schedule" which must be filed prior to becoming effective (18 C.F.R. 154.94(e)).

342 U.S. 570, 575; *United States* v. *Western Pacific R. Co.*, 352 U.S. 59, 65) has greater appreciation of the economics and usages of the natural gas industry. Since natural gas contracts typically are long, complex and technical, and reflect the industry practices that have grown up to deal with problems peculiar to the industry, the Commission's accumulated experience with the industry is of special value for the construction of these contracts.

In addition, because of the specialized nature of the industry, many contracts contain substantially identical provisions, including those relating to price. Giving the Commission primary responsibility for their interpretation will achieve the desirable aim of obtaining consistency of construction—a result that is particularly important in the producer segment of the gas industry where the contracts themselves usually constitute the rate schedules. See notes 11, 12, *supra*, p. 17. Cf. *Dobson* v. *Commissioner*, 320 U.S. 489, 499–502, where the Court stressed the need for uniformity of decision and the difficulties of otherwise achieving it as the reasons for limiting judicial review of Tax Court decisions to a determination whether they are legally and factually reasonable. The need for "the desirable uniformity which would obtain if initially a specialized agency passed on certain types of administrative questions" is also one of the principal bases for the primary jurisdiction rule. *United States* v. *Western Pacific R. Co.*, 352 U.S. 59, 64; *Far East Conference* v. *United States*, 342 U.S. 570, 574–575; see *infra*, pp. 23–26. On the other hand, the effect of permitting *de novo*

review by the various courts of appeals of the Commission's construction of such contracts would be to sacrifice the "[u]niformity and consistency in the regulation of business entrusted to a particular agency" that the "limited functions of review by the judiciary" (*Far East, supra*) are designed to accomplish.

In urging that judicial review of the Commission's construction of Shell's "favored-nation" clause be thus limited, we emphasize that the Commission was not here merely construing a contract that happened to come before it as an incident to a pending proceeding. For the Shell contract itself constituted the rate schedule, and the interpretation of such contracts is therefore an integral part of the Commission's rate regulatory jurisdiction.

B. SETTLED PRINCIPLES GOVERNING THE RELATIONSHIP BETWEEN COURTS AND AGENCIES JUSTIFY RESTRICTED REVIEW OF THE COMMISSION'S INTERPRETATION OF THE SHELL "FAVORED-NATION" CLAUSE

We submit that this Court's recent decision in *United Gas Pipe Line Co.* v. *Memphis Light, Gas and Water Division*, 358 U.S. 103, fully supports the restricted scope of judicial review of the Commission's interpretation of the Shell "favored-nation" clause here urged. The question in that case was whether the Commission had properly accepted, for filing under Section 4(d) of the Natural Gas Act, certain changes in rates for gas sold under contracts between a pipeline company and its customers. The Commission construed the contracts as obligating the customers to pay the pipeline company's "going"

rate, as established from time to time in accordance with the procedures under the Act; it further held that the Act permitted such unilateral rate changes when authorized by the contract. The court of appeals reversed, holding only that the Act did not permit such unilateral rate filings even if authorized by contract between the parties. It therefore did not reach the contract interpretation question. 250 F. 2d 402.

Since this Court disagreed with the lower court's interpretation of the Act, a ruling on the issue of contract interpretation was necessary in order completely to dispose of the controversy. This Court held that a remand to the court of appeals for consideration of that question was unnecessary, since the question involved "matters peculiarly within the area of the Commission's special competence and as to which we could hardly be aided by a further examination of the record by the Court of Appeals" (358 U.S. at 114). Limiting its discussion to only a brief mention of some of the factors supporting the Commission's interpretation, the Court ruled (*ibid.*):

> After scrutinizing the record we are satisfied that the Commission's determination as to the meaning of the service agreements here involved was amply supported both factually and legally. There is no necessity for us to embark upon a detailed discussion of the various contentions made by the parties, none of which appears to have been overlooked or misapprehended by the Commission. * * *

The question of contract interpretation in the instant case—whether the price redetermination under

the pre-existing Atlantic contract constituted the "enter[ing] into [of] a contract providing for the purchase by [the buyer] of gas" at a higher price within the meaning of the Shell "favored-nation" clause—is no less a matter "peculiarly within the area of the Commission's special competence" than the question of contract interpretation in *Memphis*. In both cases, judicial review is at an end once it appears that "the Commission's determination as to the meaning of the service agreements here involved was amply supported both factually and legally." As we show *infra* (pp. 29–39), that is the case here.

The *Memphis* case promulgated no novel doctrine. It merely applied to the Commission's construction of a contract of a natural gas company subject to Commission regulation the settled principle that an agency's interpretation of its statute, rules or regulations, resting as it does upon its expertise, will not be disturbed by the reviewing court as long as it has "'warrant in the record' and a reasonable basis in law." *National Labor Relations Board* v. *Hearst Publications,* 322 U.S. 111, 131; see *Mississippi Valley Barge Line Co.* v. *United States,* 292 U.S. 282, 286–287; *Shields* v. *Utah Idaho R. Co.,* 305 U.S. 177; *Rochester Telephone Corp.* v. *United States,* 307 U.S. 125; *South Chicago Coal & Dock Co.* v. *Bassett,* 309 U.S. 251; *Sunshine Anthracite Coal Co.* v. *Adkins,* 310 U.S. 381; *Gray* v. *Powell,* 314 U.S. 402; *Dobson* v. *Commissioner,* 320 U.S. 489; *Unemployment Compensation Commission* v. *Aragon,* 329 U.S. 143; *O'Leary* v. *Brown-Pacific-Maxon,* 340 U.S. 504; *United States* v.

Interstate Commerce Commission, 198 F. 2d 958 (C.A.D.C.), certiorari denied, 344 U.S. 893.

Thus, in the *Hearst* case, in sustaining the holding of the National Labor Relations Board that newsboys were "employees" within the meaning of the National Labor Relations Act (the court of appeals having reversed that ruling), this Court stated (p. 130):

> It is not necessary in this case to make a completely definitive limitation around the term "employee." That task has been assigned primarily to the agency created by Congress to administer the Act. Determination of "where all the conditions of the relation require protection" involves inquiries for the Board charged with this duty. Everyday experience in the administration of the statute gives it familiarity with the circumstances and backgrounds of employment relationships in various industries, with the abilities and needs of the workers for self-organization and collective action, and with the adaptability of collective bargaining for the peaceful settlement of their disputes with their employers. The experience thus acquired must be brought frequently to bear on the question who is an employee under the Act.

Similarly, in the instant case the determination of whether the Shell "favored-nation" clause was triggered by a price redetermination under an existing contract requires a "familiarity with the circumstances and backgrounds" of natural gas purchase agreements that the Federal Power Commission—but not the courts—possesses.

The expertise of administrative agencies likewise has been a critical factor in delineating the applica-

tion of the doctrine of primary jurisdiction. *Far East Conference* v. *United States,* 342 U.S. 570; *United States* v. *Western Pacific R. Co.,* 352 U.S. 59; *General American Tank Car Corp.* v. *El Dorado Terminal Co.,* 308 U.S. 422; *Thompson* v. *Texas Mexican R. Co.,* 328 U.S. 134.

In the *Western Pacific* case, *supra,* the question was whether the railroads had properly applied tariffs covering incendiary bombs to Government shipments of steel aerial bomb cases filled with an inflammatory material. The Court of Claims, although recognizing that questions as to the reasonableness of the application of tariff provisions to particular shipments were to be referred to the Interstate Commerce Commission, itself decided the question of tariff interpretation, *i.e.,* held that the bomb cases were "incendiary bombs" under the tariff. Although neither party challenged the latter ruling, this Court *sua sponte* held that the Court of Claims had erred in not referring that question to the Commission. Rejecting the view that questions of tariff construction are always "questions of law" for the court, this Court held (p. 65) that "whether * * * the Interstate Commerce Commission should first pass on the construction of the tariff in dispute here * * * depends on whether the question raises issues of transportation policy which ought to be considered by the Commission in the interests of a uniform and expert administration of the regulatory scheme laid down by the Act." It stated (pp. 66–67) that

> * * * [T]here were obviously commercial *reasons* why a higher tariff was set for incendiary bombs than for, say, lumber. It therefore fol-

> lows that the decision whether a certain item was intended to be covered by the tariff for incendiary bombs involves an intimate knowledge of these very reasons themselves. * * * Such familiarity is possessed not by the courts but by the agency which had the exclusive power to pass on the rate in the first instance. And, on the other hand, to decide the question of the scope of this tariff without consideration of the factors and purposes underlying the terminology employed would make the process of adjudication little more than an exercise in semantics. [Italics in original.]

Thus, this Court recognized that questions of tariff interpretation, although frequently characterized as "questions of law," may call for the same kind of expert knowledge and judgment as other issues that have traditionally been treated as within an agency's primary jurisdiction. In *Western Pacific,* resort to the agency was necessary because interpretation of the tariff provisions for incendiary bombs called for the Commission's "intimate knowledge of" the "commercial *reasons* why a higher tariff was set for incendiary bombs." In the instant case, proper interpretation of the Shell "favored-nation" clause—which is part of a contract filed as a rate schedule with the Commission, and therefore analogous to the tariffs involved in *Western Pacific*—likewise calls for application of the agency's expert knowledge of the significance of the various forms of such clauses used by the natural gas industry (see *infra,* pp. 31–39). Cf. also the *Memphis* case, *supra.*

In short, provisions in such natural gas supply con-

tracts, like "provisions in railroad collective bargaining agreements are of a specialized nature calling for specialized technical knowledge in ascertaining their meaning and application" (*Pennsylvania R. Co.* v. *Day*, 360 U.S. 548, 553). The Commission, and normally not the reviewing court, has the "specialized technical knowledge" that must be brought to bear in interpreting these complex agreements. The considerations that call for the referral of these specialized and technical issues to the agency in the first instance also require, we submit, that reviewing courts accept the agency's expert judgment if it has "'warrant in the record' and a reasonable basis in law" (*National Labor Relations Board* v. *Hearst Publications, supra*, 322 U.S. 111, 131).

Respondent argues (Br. in Opp. 18–24), however, that questions of contract interpretation present only questions of law; and that the reviewing court is as well qualified as the Commission to decide them. But, as we have shown (*supra*, pp. 16–25), the question whether Shell's "favored-nation" clause was triggered by the price redetermination under the Atlantic contract involves far "more than simply a question of reading the [contract] language or applying abstract 'rules' of construction" (*Western Pacific, supra*, p. 67). Rather, it requires the kind of expertise that "is possessed not by the courts but by the agency * * *" (*ibid.*).

This Court has pointed out (*Dobson* v. *Commissioner*, 320 U.S. 489, 501) "the want of a certain standard for distinguishing 'questions of law' from 'questions of fact,'" and has recognized the dangers

of attempting to define the scope of judicial review of administrative action on the basis of so tenuous a distinction. Thus, in *O'Leary* v. *Brown-Pacific-Maxon,* 340 U.S. 504, the Court reviewed a determination by a Deputy Commissioner under the Longshoremen and Harbor Workers Act that a deceased employee's death "arose out of and in the course of his employment." In affirming the Deputy Commissioner's award, the Court stated (340 U.S. at 507–508):

> The Deputy Commissioner treated the question whether the particular rescue attempt described by the evidence was one of the class covered by the Act as a question of "fact." Doing so only serves to illustrate once more the variety of ascertainments covered by the blanket term "fact." Here of course it does not connote a simple, external, physical event as to which there is conflicting testimony. The conclusion concerns a combination of happenings and the inferences drawn from them. In part at least, the inferences presuppose applicable standards for assessing the simple, external facts. Yet the standards are not so severable from the experience of industry nor of such a nature as to be peculiarly appropriate for independent judicial ascertainment as "questions of law."

The scope of judicial review of agency action does not turn, we submit, upon technical distinctions between "questions of fact" and "questions of law" and it is therefore immaterial that, in other contexts and for other purposes, questions of contract interpreta-

tion are characterized as questions of law. For the scope of review depends upon a realistic analysis of whether the issue decided by the agency is so within its expert competence as to make it inappropriate for the reviewing court to substitute its judgment for that of the agency. Cf. *Western Pacific, supra.*[13] Indeed, even such "questions of law" as issues of statutory interpretation have sometimes been left to agency determination with but limited review by the courts.[14] Such a restricted scope of judicial review of matters which agencies are better qualified to resolve than courts best effectuates the basic tenet of administrative law that

> * * * [I]n construing a statute setting up an administrative agency and providing for judicial review of its action, court and agency are

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[13] See Landis, *The Administrative Process* (1951), p. 152; Brown, *Law and Fact in Judicial Review* (1943), 56 Harv. L. Rev. 899, 921–928; Cooper, *Administrative Justice and The Role of Discretion* (1938), 47 Yale L. Journal 577, 588–590; Paul, *Dobson* v. *Commissioner: The Strange Ways of Law and Fact* (1944), 57 Harv. L. Rev. 753, 803, *et seq.*; Stern, *Review of Findings of Administrators, Judges and Juries: A Comparative Analysis* (1944), 58 Harv. L. Rev. 70, 99–109; Report of The Attorney General's Committee on Administrative Procedure (1941), pp. 88–90.

[14] See, *e.g.*, *National Labor Relations Board* v. *Hearst Publications*, 322 U.S. 111 ("employees"); *Shields* v. *Utah Idaho R. Co.*, 305 U.S. 177 ("interurban railway"); *Sunshine Anthracite Coal Co.* v. *Adkins*, 310 U.S. 381 ("bit..minous" coal); *Rochester Telephone Corp.* v. *United States*, 307 U.S. 125 ("control" of a company); *South Chicago Coal & Dock Co.* v. *Bassett*, 309 U.S. 251 ("member of the crew"); *Unemployment Compensation Commission* v. *Aragon*, 329 U.S. 143 ("labor dispute in active progress"). See Jaffe, *Judicial Review: Question of Law* (1955), 69 Harv. L. Rev. 239.

> not to be regarded as wholly independent and unrelated instrumentalities of justice, each acting in the performance of its prescribed statutory duty without regard to the appropriate function of the other in securing the plainly indicated objects of the statute. Courts and agency are the means adopted to attain the prescribed end, and so far as their duties are defined by the words of the statute, those words should be construed so as to attain that end through coordinated action. [*United States* v. *Morgan*, 307 U.S. 183, 191.]

II

THE COMMISSION'S CONSTRUCTION OF THE SHELL "FAVORED-NATION" CLAUSE AS NOT APPLICABLE TO PRICE REDETERMINATIONS UNDER PRE-EXISTING CONTRACTS WAS REASONABLE

The Shell "favored-nation" clause provides that if at any time after December 31, 1951, Texas Gas "shall enter into a contract providing for the purchase by it of gas" at a higher price,[15] the price under the Shell contract shall be increased to the "price payable under such other contract" (R. 66-67). When the Shell contract was executed on May 1, 1951, Texas Gas was also a purchaser under a long-term contract with The Atlantic Refining Company ("Atlantic"). The Atlantic contract, executed in 1943, provided in Paragraph III for periodic price redeterminations every five

[15] The clause applies only to contracts for the purchase of gas to be produced and delivered from fields within a 50-mile radius of any gas delivered under the Shell contract (R. 67). It was stipulated that the delivery point under the Atlantic contract is within that radius (R. 15, 120).

953, the price paid by Texas Gas
eased, as reflected in a letter be-
d Atlantic which stated that the
"In accordance with Paragraph
(R. 46).

construing the Shell "favored-na-
licable only where Texas Gas en-
contract for the purchase of gas,
. 132) that the 1953 "agreement
ot constitute a new contract as re-
calation clause, but merely repre-
under a pre-existing contract be-
nd Atlantic." And, in its order
he Commission, referring to other
tracts in the record, pointed out
re Shell and its buyer did intend
e place when prices were raised
new contracts, language was used
e this result * * *."

show, this interpretation by the
Shell "favored-nation" clause was
nable, for it reflects the signifi-
the natural gas industry between
auses that are triggered whenever
igher price and those that are trig-
ich higher price is the result of a
contract. Moreover, it furthers
licy of the Natural Gas Act to pro-
consumers of natural gas against

A. THE SHELL "FAVORED-NATION" CLAUSE WAS NOT INTENDED TO COVER PRICE REDETERMINATIONS UNDER PRE-EXISTING CONTRACTS

1. *There is a basic difference in economic effect between natural gas "favored-nation" clauses that are triggered by the payment of any higher price, and those triggered only when the buyer enters into a new contract.* In construing the Shell "favored-nation" clause, the court of appeals stated (R. 163) that the "usual objective of such a clause is to assure the seller a top price for its gas." This general statement, however, overlooks the fact that, because of the particular business problems of the natural gas industry, several variations in these clauses have developed in that business. The Commission, with its specialized knowledge of the industry, was particularly well qualified to appreciate the significance of these variations.

Basic to the problem of negotiating gas supply contract between producers and pipelines is the fact that the Commission, in order to protect the public dependent upon the gas being supplied, will not authorize a pipeline to undertake new service without assurance of an adequate long-term supply of gas; and that without such gas supply lending institutions will not provide the large amounts of capital necessary to finance the heavy investment required for major pipeline construction. For this reason, most gas purchase contracts between producers and pipelines are long-term, typically of 20-years duration, or more.[16]

[16] The court below (R. 163) relied on testimony by a Shell witness (R. 13) that at the time Shell negotiated the Texas Gas contract, it "hadn't * * * before" given a 20-year contract. The Commission did not so find, and at that time Shell already had

From the producers' viewpoint, however, a long-term gas sales contract at a fixed price may be disadvantageous—particularly in periods of rising gas prices, such as this country has experienced since World War II.

These conflicting interests were resolved by providing for future price increases in long-term contracts. Such provisions take various forms. At an earlier period, when the demand for gas did not equal the supply, the contracts typically provided for periodic price increases at a fixed amount agreed upon in advance. Later, however, so-called "indefinite pricing" clauses came into widespread use.[17] These clauses

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a number of 20-year contracts covering that area. Seven such contracts are part of the present record. These contracts were offered in evidence at the administrative hearings by reference to the files of the Commission, and are set forth at the following pages of the record certified by the Commission to the court of appeals, pursuant to Rule 18(7) of the Rules of that court: 438, 630, 1030, 1235, 1280, 1449, 1747. In accordance with that rule, the record was not physically transmitted to the court, but is being held by the agency, and is available upon request.

[17] These clauses include, in addition to the two-party "favored-nation" clause here involved, the third-party "favored-nation" clause, the "price redetermination" clause, and the "spiral escalator" clause. Under the third-party "favored-nation" clause, the price is increased whenever a higher price is paid to another producer by any one not a party to the contract. The "price redetermination" clause provides for an increased price at periodic intervals based generally upon the average of the two or three highest prices being paid for gas in a defined area. Under the "spiral escalator" clause, the price is increased in a prescribed proportion to any increase in the resale price charged by the

do not specify the amount of future increases, but make them depend upon various factors, such as the general price level in the market area, the extent to which other producers raise their prices, etc. One of the most widely-used of such provisions is the "favored-nation" clause, under which the price increase is tied to the payment of higher prices by the buyer to other sellers.

As a result of the bargaining process between the selling producer and the purchasing pipeline company, "favored-nation" clauses in use today in the natural gas industry typically vary in scope. One common variation from the basic clause, under which the price is triggered automatically whenever the buyer pays a higher price for gas in the defined area,[18] is a provision limiting the triggering to situations where (as in the instant case) the buyer pays a higher price for gas under a subsequently entered-into contract. The language utilized in providing for these different kinds of price escalations is significantly different (see *infra,* pp. 36–37), and the two types reflect a basic difference in economic and business purpose.

Pipeline negotiations for new gas are necessarily conducted in the context of existing supply arrangements and with the knowledge that the pipeline will be seeking further new gas supplies in the future. A pipeline's existing contracts typically contain one

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purchasing pipeline. See H. Rep. No. 992, 84th Cong., 1st Sess., pp. 8–9.

[18] The scope of the geographical area in which a "favored-nation" clause is applicable varies from contract to contract depending on the parties' agreement.

or more definite or indefinite escalation clauses, and the pipeline is aware that it must accept some kind of escalation clause in order to obtain any long-term commitment. From the pipeline's point of view, a "favored-nation" clause that is triggered only when the buyer enters into a new gas-purchase contract is highly desirable because it gives the pipeline some measure of control over increases in the cost of its existing gas supply. That is, under such a clause the pipeline itself makes the business judgment that increases its gas price under existing contracts, *i.e.*, by entering into new supply contracts in the area.

Since the costs of constructing new transmission facilities are substantial, a pipeline tends to purchase new gas requirements in its existing supply areas, from which it already has adequate transmission service. Under the "new-contract" type of "favored-nation" clause, a pipeline considering expansion can balance the costs of buying new gas in its present supply areas (and thereby triggering the price increase in its existing contracts) against the costs of obtaining the new gas in other areas.

Moreover, such "new-contract" clauses enable the pipeline to determine the timing of escalated price-increases. Price escalations under an existing contract typically are fixed by the terms of that contract; for example, the Atlantic contract provided for price redetermination every five years. And since existing contracts have been entered into at various times in the past, the occurrence of price increases under such clauses are widely spread in time. In contrast, when the "favored-nation" clauses are limited to future

contracts, the pipeline under certain conditions may control price escalations by selecting the precise date on which it enters into a new contract at a higher price.

Such control over timing is valuable to a pipeline because, as a natural gas company subject to regulation under the Natural Gas Act, it can pass on its increased costs only after filing a proposed increased rate with the Commission, and Commission review thereof. It is thus impracticable for a pipeline to increase its rates with every increase in its costs. By controlling the timing of cost increases, and thus limiting their frequency, a pipeline may be able to minimize the number of rate increases that it has to file with the Commission.

On the other hand, a "favored-nation" clause that becomes operative whenever the buyer pays a higher price for gas in the same area (for whatever reason) leaves the pipeline with no control over either the occurrence or the timing of price increases in its existing supply. Thus, to whatever extent a pipeline can limit the "favored-nation" clause in the contract currently being negotiated, it maintains some control of future price increases under that contract.

From the seller's standpoint, the distinction between "new contract" "favored-nation" clauses and those operative whenever the buyer pays a higher price under existing contracts similarly rests on sound business considerations. At the time of contracting, the seller can bargain directly for substantive concessions in its own contract similar to those in the buyer's existing contracts with other producers. Its

claims for parity as against existing contracts can thus be directly negotiated and compromised, so that only the function of assuring equality with future contracts, the terms of which cannot then be known, need be left to the "favored-nation" clause. Thus, restricting the operation of "favored-nation" clauses of the type here involved to situations where the buyer enters into a new contract for the purchase of gas is in no way unfair to the seller. He has good bargaining position, and he gets precisely what he bargained for.

2. *The Commission correctly construed the Shell "favored-nation" clause here involved as triggered only by the execution of a new contract for the purchase of gas.* In view of the Commission's knowledge of the foregoing practical economic considerations bearing upon the negotiation of natural gas supply contracts,[19] we submit that the Commission was fully justified in holding that the Shell "favored-nation" clause was triggered only when Texas Gas entered into a new contract for the purchase of gas, and not upon a mere price redetermination under an existing contract. For, as the Commission pointed out (R. 147) in denying rehearing, other gas sales contracts that Shell had also filed with the Commission as rate schedules used specific language when it was "intend[ed] that escalations take place when prices were raised under either old or new contracts * * *"—language which unequivocally states that the price is to be increased at any time that the buyer pays a

[19] It is these factors, rather than those conjectured by the court below (R. 163–164), that constitute the "business practicalities" (R. 164) in the light of which the Shell contract must be construed.

higher price for gas. For example, the "favored-nation" clause in Shell's contract with Tennessee Gas Transmission Company (Shell Gas Rate Schedule No. 6), executed on February 23, 1951, about two months prior to the contract here involved, provides (R. 106; emphasis added):

> If *at any time the cost per MCF of gas purchased by Buyer from any gas producer whomsoever* * * * *shall be greater* than the cost per MCF of gas purchased hereunder, Buyer will increase the price per MCF payable to Seller for gas delivered hereunder * * *.

The broad phrase "at any time" appears again in the comparable provision of Shell's Gas Rate Schedule No. 4, which likewise provides (R. 147; emphasis added):

> If *at any time or times the price per MCF of gas or dry gas purchased by [the Buyer] from any gas producer whomever* * * * *shall be greater* than the price per MCF of gas purchased hereunder, [the Buyer] will increase the price per MCF payable to [Shell] for gas delivered hereunder * * *

Shell's Rate Schedule No. 10 (R. 107) explicitly provides for a price increase where the buyer pays a higher price under either an existing or future contract. It states:

> If Buyer has entered into or should hereafter enter into a contract at any time or from time to time for the purchase of gas * * * and such contract provides a price to be paid for such gas during any year, which differs from the price payable under this contract during the same year * * *.

Gas purchase contracts involve substantial sums, they are complex and technical documents, and they are usually the subject of protracted negotiations between the parties. The Shell contract in the instant case is a lengthy document (R. 57–71), obviously prepared with careful attention to many details. If the parties had intended the "favored-nation" clause in this contract to have been operative whenever the buyer merely paid a higher price under an existing contract, it is reasonable to suppose that they would have used language similar to that employed in other Shell contracts that clearly so provides—phrases such as "If at any time the cost" increases, or "If Buyer has entered into or should hereafter enter into a contract" for the purchase of gas at a higher price.

Instead, however, the parties chose to employ terminology that points in precisely the opposite direction: "If at any time after December 31, 1951, Buyer shall enter into a contract providing for the purchase by it of gas" at a higher price, the price payable under the Shell contract shall "equal the price payable under such other contract" (R. 66–67). In the light of the significant differences between the economic consequences of the two types of clauses, and the sharp difference in language between the instant clause and other clauses of Shell contracts on file with the Commission, we submit that the Commission was plainly reasonable in construing the instant contract as meaning what it obviously intended: namely, that the price increase would be triggered only if Texas Gas there-

after entered into a new contract for the purchase of gas.

3. ***The price redetermination under the Atlantic contract did not constitute the "enter[ing] into" of a new gas-purchase contract within the meaning of the Shell "favored-nation" clause.*** The Commission correctly ruled that the price redetermination under the Atlantic contract did not constitute the "enter[ing] into" of a new contract within the meaning of the Shell "favored-nation" clause. For, as the Commission pointed out (R. 132; see R. 130), the "letter agreement" between Texas Gas and Atlantic that redetermined the price (R. 46) was not "a new contract for the purchase of gas," but was merely "action taken pursuant to the pre-existing 1943 Atlantic contract."

In view of the business considerations previously discussed that underlie the negotiation of "favored-nation" clauses in the natural gas industry (*supra,* pp. 31–36), we submit that the parties to the Shell contract did not intend that a price redetermination under a pre-existing gas contract of Texas Gas would escalate prices under the Shell contract. Such a price increase was not a matter over which Texas Gas had control. The price under the Atlantic contract was subject to renegotiation every five years, and if the parties were unable to agree upon a new higher price, the contract provided for its fixing through compulsory arbitration. The question is discussed at greater length in Point III, *infra,* pp. 42–50, where we point out the errors of the contrary ruling by the court of appeals.

B. THE COMMISSION'S INTERPRETATION OF THE SHELL "FAVORED-NATION" CLAUSE FURTHERS THE PURPOSE OF THE NATURAL GAS ACT TO PROTECT THE ULTIMATE CONSUMERS

As this Court has pointed out, "The primary aim of this legislation was to protect consumers against exploitation at the hands of natural gas companies." *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591, 610; see *Federal Power Commission* v. *Interstate Natural Gas Co.*, 336 U.S. 577, 581; *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672, 685. The necessary effect of "favored-nation" clauses is to increase the price of natural gas in the field, and hence its price to the ultimate consumers (see *infra*, pp. 40–41). The Commission's construction of the Shell clause, which limits its operation to situations where the buyer enters into a new supply contract, thus furthers the policy of the Act by minimizing the clause's inflationary impact. On the other hand, the court of appeals' construction, which results in higher prices whenever the buyer merely pays a higher price under an existing contract providing for price redeterminations, inevitably and unnecessarily increases prices to the ultimate consumers.

Typically, the event which triggers a "favored-nation" clause is the payment by the pipeline of a higher price. But since the reasons for this higher price relate solely to the situation of the new seller, price increases under such clauses are unrelated to the costs, financial needs, or other economic factors of the producer whose rates are thereby escalated. The deleterious effect of these clauses upon the consumer interest is furthered by the fact that under

them the current producer price is escalated not to the average price in the field nor even to the generally prevailing price, but to the highest price being paid by the pipeline. As a result, "favored-nation" clauses not only exert a strong upward pressure upon producer prices, but also tend to increase the prevailing market price in the area.

Since the purpose and effect of these clauses is always to raise the producer price, never to reduce it, these clauses never operate in the interest of the consumers.[20] Accordingly, any proper restriction upon

[20] The serious effect of "favored-nation" clauses upon natural gas consumers was recognized by both the proponents and the opponents of the legislation passed in the 84th Congress to exempt producers from regulation under the Natural Gas Act. See Hearings before the House Interstate and Foreign Commerce Committee on H.R. 4560, 84th Cong., 1st Sess., pp. 82–87, 1543; Hearings before the Senate Interstate and Foreign Commerce Committee on S. 712, *et al.*, 84th Cong., 1st Sess., pp. 134–137, 1593–1619. The bill that Congress enacted (which the President vetoed for other reasons (see H. Doc. No. 342, 84th Cong., 1st Sess.; 102 Cong. Rec. 2897–2898)) contained various prohibitions and restrictions upon the use of "favored-nation" clauses. H.R. 6645, 84th Cong., 1st Sess. In proposing such limitations, the House Committee stated (H. Rep. No. 992, 84th Cong., 1st Sess., p. 9):

> Many witnesses appearing before the Committee, particularly those representing distributing interests and consumer areas, maintained that escalation clauses in existing contracts, unless their operation is controlled in some effective manner, could result in very large increases in the cost of gas to consumers—particularly in view of the fact that a contract for natural gas usually runs for 20 years or more, and a large proportion of the contracts presently in effect were entered into in recent years.

The Senate bill (S. 1853) contained similar provisions "designed to give the consumer further protection against unwarranted price increases due to escalation clauses." S. Rep. No. 1219, 84th Cong., 1st Sess., p. 9; see also pp. 7–9, 11–12, 22.

the scope of such clauses necessarily favors the consumer interest which the Act is designed to protect.

III

EVEN IF THE QUESTION WHETHER THE ATLANTIC PRICE REDETERMINATION TRIGGERED THE SHELL "FAVORED-NATION" CLAUSE WERE OPEN TO DE NOVO JUDICIAL EXAMINATION, THE COURT OF APPEALS' RULING IS ERRONEOUS

In Points I and II. *supra,* we have shown that, upon judicial review of the Commission's interpretation of the Shell "favored-nation" clause contained in a rate schedule filed with the agency, the court of appeals is limited to determining whether the Commission's construction is reasonable; and that the Commission's ruling that the Atlantic price redetermination did not trigger the Shell price rise, based as it was upon the agency's expert knowledge of the natural gas business, satisfies that standard. We shall now show that, even if the matter were deemed subject to *de novo* judicial examination, the court of appeals nevertheless erred in holding that the Shell price was escalated when the Atlantic price was increased.

A. THE SHELL "FAVORED-NATION" CLAUSE APPLIES ONLY WHEN THE BUYER ENTERS INTO A NEW GAS-SUPPLY CONTRACT, AND NOT WHEN THE PRICE UNDER A PRE-EXISTING CONTRACT IS REDETERMINED

The arguments presented in Point II, *supra,* to support the reasonableness of the Commission's holding that the Shell "favored-nation" clause is triggered only by the execution of a new gas-purchase contract

also establish the correctness of that ruling as an independent question of law. The clear distinction between the other Shell clauses that, in terms, apply whenever the buyer pays a higher price under existing or future contracts (*supra,* pp. 36–37) and the instant clause, which is activated only if, at some future date, the "Buyer shall enter into a contract" for the purchase of gas at a higher price (R. 66–67), shows that the two types of clauses are not the same. We submit that the parties' use of the latter, rather than the former, type of clause in the instant agreement was not inadvertent. On the contrary, it clearly manifested their intent that Texas Gas was not to pay a higher price under the Shell contract merely because it thereafter paid a higher price for gas, but only when such higher price was the result of its thereafter "enter[ing] into" a new contract for the purchase of gas.

As noted (*supra,* pp. 31–36), such a limitation reflects the basic economics of the natural gas business. The statement of the court below (R. 163) that the parties intended that "any higher price paid by [the buyer] to another producer [was] to trigger a rise on the Shell contract to the same figure except possibly where a pre-existing contract already provided for a settled step-up in price" ignores the clear distinction between the two types of "favored-nation" clauses shown by the record.[21]

[21] Moreover, there is no basis either in the provisions of the Shell contract, or in the record, for the court's exception in cases "where a pre-existing contract already provided for a settled step-up in price."

IC PRICE REDETERMINATION WAS NOT THE ENTERING
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ling that the Atlantic price redetermina-
ed the Shell price, the court of appeals
question as turning on the legal characteri-
e former, *i.e.*, was the Atlantic price rede-
itself a "contract for the purchase of
whether the Atlantic redetermination esca-
hell price is a question of the intent of
to the Shell contract, *i.e.*, what events did
would escalate the Shell price. The criti-
erefore, is not how the Atlantic redetermi-
ht be characterized as an independent
contract law in some other context, but
parties to the Shell contract, in agreeing
ire-contract" limitation, intended it to ex-
e redeterminations covering gas furnished
xisting supply arrangements. As we have
circumstances surrounding the transaction
t the parties to the Shell contract intended
ereunder to escalate only when the buyer
ntered into a new supply contract. See
1–39.

event, we submit that the court below
cluding that, as a matter of contract law,
price redetermination itself constituted a
ontract * * * for the purchase * * * of
court predicated this conclusion on the
at the Atlantic price redetermination was
agreement of the parties rather than by
that such an agreement is a "contract":

that the "purchase" of gas could not be completed until the price was established; and that, therefore, the price redetermination was a "contract providing for the purchase * * * of gas" entered into after the specified date in the Shell clause (R. 164). But examination of the 1943 Atlantic contract and the letter setting forth the 1953 redetermination shows (1) that the 1943 contract created a long-term commitment for the purchase of gas which remained in effect whether or not the parties were able to agree upon a new price at periodic intervals; and (2) that the 1953 price redetermination was not a gas purchase "contract" separate and distinct from the basic 1943 contract, but rather was a step taken in performance of the latter in accordance with its explicit provisions.

By its terms, the duration of the 1943 contract does not depend upon the successful renegotiation of the price thereunder, but upon the continued existence of the supply of gas. Condition X of the contract provides (R. 90–91):

> The rights of the parties hereunder shall continue in force and effect for the gas producing life of the North Tepetate Pool but in any event not to exceed twenty-five (25) years, unless sooner terminated by mutual consent or pursuant to the specific rights of termination herein elsewhere set forth.

Since there is no claim that the contract has been terminated by mutual consent or that the gas-producing life of the North Tepetate Pool has expired, the 1943 contract plainly was in full force and effect at

This view of the 1943 contract as a single long-term agreement with provisions for periodic price adjustment, rather than as a five-year contract periodically renewable if the parties agree upon a new price, accords with the normal industry practice of employing long-term contracts (see *supra,* pp. 31–32). It is further supported by the provisions in that contract for price redetermination which, we believe, make it explicit that the agreement continues whether or not the parties can agree upon new prices. After providing for price adjustments by agreement of the parties, the contract states (Condition III(d), R. 86):

> In the event that the parties are unable to agree upon the price to be paid for gas after the first five-year period, in accordance with the arrangements set forth in paragraphs (b) and (c) above, such determination shall be submitted to arbitration in accordance with Condition XII.

Thus, the continued operation of the contract is made completely independent of the parties' ability to agree upon a new price. For if they cannot do so, the only effect is that the matter then goes to arbitration. Their respective contractual obligations to supply and to buy gas, however, continues. By agreeing upon a new price the parties did not, as the court of appeals stated (R. 164), "[give] up their rights under the original contract to proceed to arbitration." Rather, they were carrying out the contractual provisions for price adjustment by the parties, and thus making it unnecessary to invoke the alternative price-fixing device of arbitration.

The letter which sets forth the 1953 price redetermination (R. 46) further shows that the redetermination was not a new gas-purchase contract, "but merely represents action taken under a pre-existing contract" (R. 130). This single-page document contains none of the myriad of details normally found in a gas contract (compare R. 57–71, 81–94), and does not purport to be in substitution for the 1943 agreement. On the contrary, it recognizes the continuing validity of that agreement. For, after referring in general terms to the 1943 contract, it provides (R. 46; emphasis added):

> *In accordance with Paragraph III of said contract,* it is hereby agreed that the price * * * for gas sold and delivered under such contract between September 1, 1953, and August 31, 1958, [the five-year period prescribed by the 1943 contract] shall be * * *.

In *Phillips Petroleum Co.* v. *Federal Power Commission,* 227 F. 2d 470 (C.A. 10), certiorari denied, 350 U.S. 1005, the question was whether the Commission had properly suspended certain rate schedules filed by a natural gas producer. This depended upon whether two letter agreements between the producer and the pipeline, providing for increased rates "[i]n accordance with the 'formula [in the escalator clause] in the contract' " between them (227 F. 2d at p. 472), were part of the basic contract or whether they constituted a separate agreement. The court held (p. 476) that "the original contract, as amended, together with the letter agreements are all integrated parts of one contract." It pointed out (p. 475; emphasis

> was being paid not by force of letter agreements, but by force of the binding effect of the escalator clauses which operated to fix the prescribed rate in accordance with the formula in the contract. *The letter agreements were merely executory of the contracts between the parties.*

This reasoning, we submit, is equally applicable to the instant case.

Shell's actions after learning of the Atlantic price redetermination further indicate that the parties did not intend that such a price adjustment would trigger the Shell "favored-nation" clause. Although Shell learned about the Atlantic price increase in March, 1954 (R. 16), it did not notify Texas Gas that it was claiming the increased price until more than six months later, in October, 1954 (R. 35). Moreover, in its original rate filing with the Commission in November, 1954, Shell did not show the higher Atlantic rate as its effective rate on June 7, 1954. Instead, it filed the Shell contract showing the old rate, together with a "sample" billing at the higher rate (R. 80, 110, 127). When the Commission requested an explanation (R. 151), Shell waited more than two years before presenting to the Commission its justification for the higher rate (R. 72–77). From March, 1954, to February, 1957, the credit memoranda submitted by Texas Gas and its checks in payment for the gas under the Shell contract uniformly set forth, and were based upon, the unescalated price provided by that contract (8.997¢ per Mcf) (R. 48–50). In accepting those checks over this extended period, Shell never attempted to pre-

of seven statements made by Shell during this period to public accountants who were auditing the books of Texas Gas and its predecessor, Shell stated that balances due to it as shown by such books, which were calculated on the basis of the unescalated price, were correct (R. 50–57).

The court of appeals' characterization of the price redetermination as "fit[ting] best into the rubric of an accord itself taken as satisfaction" (R. 164) is unsound. An "Accord and satisfaction is the discharge of a contract, or a disputed claim arising either from a contract or from a tort, by the substitution of an agreement between the parties in satisfaction of such contract or disputed claim * * *." *Nelson* v. *Chicago Mill & Lumber Corp.*, 76 F. 2d 17, 23–24 (C.A. 8); see also, *General Foods Corp.* v. *The Felipe Camarao*, 172 F. 2d 131, 133 (C.A. 2), certiorari denied, 337 U.S. 908; *Whiting Stoker Co.* v. *Chicago Stoker Corp.*, 171 F. 2d 248, 252 (C.A. 7), certiorari denied, 337 U.S. 915; *Sinclair Refining Co.* v. *Gutowski*, 195 F. 2d 637, 640 (C.A. 6), certiorari denied, 344 U.S. 821; 6 Corbin, *Contracts* (1951 ed.) § 1276. Here, there was no discharge of the 1943 contract and the 1953 single-page letter agreement was not in substitution for the original contract. It was "merely executory of the contract between the parties" (*Phillips, supra*) which provided for periodic rate adjustments at five-year intervals, to be determined either by agreement of the parties or, if that failed, by arbitration.[22]

[22] The absence of any precise formula for redetermining the price does not, as Shell apparently suggests (Br. in Opp. 16–17), make the Atlantic contract unenforceable, and thus convert every price readjustment into a new purchase con-

The error in the court of appeals' ruling is further shown by the court's apparent recognition that, if the parties to the Atlantic contract had failed to agree in 1953 and the new price had been fixed by arbitration, no new gas-purchase contract would have resulted (see R. 164). But the parties to the Shell contract, and particularly Shell, obviously did not intend that Shell's right to a higher price would depend on the fortuity that the new Atlantic price was fixed by agreement rather than through arbitration. The correct interpretation of the Shell agreement, we submit, is that the parties used language which meant what it says, namely, that the price thereunder would be increased only if the buyer thereafter entered into a new contract for the purchase of gas. The Atlantic price redetermination, made pursuant to the specific provisions therefor in the Atlantic contract, did not constitute a new gas-purchase contract.

---

tract. The Atlantic contract provided that the redetermined prices were to be agreed upon "after a survey of prevailing prices for gas being sold in similar quantities in the southwestern part of Louisiana" (R. 86). This was obviously the touchstone for determining the prices, and it was a sufficiently definite standard. See, *e.g.*, *Cities Service Gas Producing Co.* v. *Federal Power Commission*, 233 F. 2d 726, 730 (C.A. 10), certiorari denied, 352 U.S. 911; *Col-Tex Refining Co.* v. *Coffield & Guthrie, Inc.*, 196 F. 2d 788 (C.A. 5). In any event, any otherwise fatal vagueness was cured by the provision for arbitration if the parties failed to agree. *Texas Co.* v. *Z. & M. Independent Oil Co.*, 156 F. 2d 862, 866–867 (C.A. 2); *United Fuel Gas Co.* v. *Columbian Fuel Corporation*, 165 F. 2d 746 (C.A. 4); *Aitchison* v. *Anderson*, 183 F. 2d 922, 925 (C.A. 9). Moreover, the parties to the contract treated it as enforceable, and under its standards were able to reach agreement on price increases both in 1948 and 1953, without having to resort to arbitration.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the judgment of the court of appeals should be reversed and that the Commission's order, holding that the Atlantic price redetermination did not escalate the Shell price, should be reinstated.

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MARCH 1960.

APPENDIX

The Natural Gas Act, 52 Stat. 821, as amended, 15 U.S.C. 717, *et seq.*, provides in pertinent part as follows:

> SEC. 4(c): Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from the date this Act takes effect [June 21, 1938]) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services. [15 U.S.C. 717c(c).]
>
> SEC. 4(d): Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and

the time when they shall take effect and the manner in which they shall be filed and published. [15 U.S.C. 717c(d).]

SEC. 19(b): Any party to a proceeding under this Act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be transmitted by the clerk of the court to any member of the Commission and thereupon the Commission shall file with the court the record upon which the order complained of was entered, as provided in section 2112 of title 28, United States Code. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced

upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the Judicial Code, as amended (U.S.C., title 28, secs. 346 and 347). [15 U.S.C. 717r.]

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1959.

Nos. 167 and 170.

TEXAS GAS TRANSMISSION CORPORATION AND LOUISVILLE GAS AND ELECTRIC COMPANY AND FEDERAL POWER COMMISSION,
Petitioners,

v.

SHELL OIL COMPANY,
Respondent.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF OF SHELL OIL COMPANY.

Opinion and Orders Below.

The opinion of the Court of Appeals (R. 160-165) is reported at 263 F. 2d 223. The order of the Federal Power Commission (R. 126-137) is reported at 18 F. P. C. 617; denial of rehearing (R. 143-150) is reported at 19 F. P. C. 74. The decision of the Presiding Examiner is in the record (R. 112-126).

Questions Presented.

The price escalation clause in a 1951 gas sale contract between Shell and the pipe line becomes "immediately" operative should the pipe line thereafter "enter into a contract providing for the purchase by it of gas" at a higher

price. On February 17, 1954, when Shell was receiving 8.997 cents per Mcf for its gas, the pipe line, after extensive negotiations with another producer (Atlantic Refining Company), entered into an agreement with Atlantic agreeing upon the purchase price of 12.5 cents per Mcf for gas to be sold by Atlantic to the pipe line for the period September 1, 1953 to August 31, 1958. This 1954 agreement resulted from a prior gas purchase contract which had an established price for the first five years but which, for each five year period after the first five years, did not establish a fixed price but required (R. 86) "Buyer and Seller are to reach an agreement as to price. . . . The price . . . is to be agreed upon at the beginning of such [five year] period after a survey of prevailing prices for gas being sold in similar quantities in the southwestern part of Louisiana." Arbitration could be resorted to if the parties were unable to agree upon the price.

After a dispute arose between Shell and the pipe line as to whether the February 1954 agreement between the pipe line and Atlantic was a contract which activated the price clause in the Shell contract, and pursuant to the Commission's 1954 regulations requiring producers' contracts to be filed as rate schedules (18 C.F.R. 154.91, *et seq.*), Shell filed its 1951 contract with the Commission. In a proceeding convened by the Commission to determine Shell's "properly effective" June 7, 1954 price, the Presiding Examiner concluded that the February 1954 agreement activated the Shell clause. The Commission reversed the Examiner and held that the Shell clause required a "new" contract and that the 1954 agreement between the pipe line and Atlantic was not a "new" contract but was "merely action taken pursuant to a pre-existing contract". The Court of Appeals held the February 1954 agreement

was a contract within the contemplation of and hence activated the Shell clause. Accordingly, the Court vacated the Commission's order and remanded to the Commission to ascertain whether the price in the February 1954 contract was indeed higher than the Shell price.

The questions presented are:

1. Whether, in these circumstances, the Court of Appeals exceeded its power in reviewing the *correctness* of the Commission's determination.

2. Whether the Court of Appeals was correct in deciding that the February 1954 agreement constituted entry into a contract within the meaning of the Shell price clause.

Statutes Involved.

Section 19(b) of the Natural Gas Act (52 Stat. 831, 15 U. S. C. 717r(b)) and Section 10(e) of the Administrative Procedure Act (60 Stat. 243, 5 U. S. C. 1009(e)) are printed as Appendices A and B hereto.

Statement.

(a) Nature of the Proceeding.

This proceeding was instituted by the Federal Power Commission for the purpose of determining Shell's legally effective rate as of June 7, 1954[1] for natural gas produced in the Chalkley Field, Cameron Parish, Louisiana and sold by Shell to Louisiana Natural Gas Corporation[2] under a

---

[1] The date as of which the Commission asserted jurisdiction over the prices of independent producers of natural gas following *Phillips Petroleum Company* v. *Wisconsin*, 347 U. S. 672 (1954).

[2] The contract was between Shell, as Seller, and Louisiana Natural, as Buyer. By merger in June, 1955, Texas Gas Transmission Corporation, a petitioner here, succeeded to all the rights and obligations of Louisiana Natural under the contract. The purchaser under this contract will be referred to generally as the pipe line, and sometimes as Louisiana Natural or Texas Gas, depending upon which was the purchaser at the time of the event being discussed.

contract dated May 1, 1951. The contract is on file with and has been accepted by the Commission as Shell's F.P.C. Gas Rate Schedule No. 153 (R. 57-71; 152-159).

Pursuant to the Commission's regulations (18 C. F. R. 154.91, *et seq.*), Shell filed with the Commission the May 1, 1951 contract. The filing was accompanied by a credit statement furnished to Shell by the purchaser[3] covering deliveries of gas for the month of May, 1954 (R. 81). This statement shows that payments as of that time were being made on the basis of 8.997¢ per Mcf. The filing was also accompanied by a sample billing showing Shell's June 7, 1954 price to be 12.5¢ per Mcf instead of 8.997¢ per Mcf (R. 80). This latter statement contains the following notation (R. 80):

> "We [Shell] claim the contract price is 12.5¢ per Mcf. (effective from September 1, 1953), but we have received only 8.997¢ per Mcf. This matter is now under negotiation with purchaser."

On February 11, 1957 Shell filed an application for a rate increase from 12.5¢ to 16.75¢ per Mcf[4] (R. 72-77). In this filing Shell explained the basis for its position that the legally effective rate on June 7, 1954 was 12.5¢ per Mcf, the basis being that under the price escalation clause in its contract, the price had automatically increased to that figure prior to June 7, 1954, by virtue of the February 17, 1954 agreement.

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[3] The contract did not provide for Shell to bill the purchaser for gas sold. Instead the contract required, and the practice was, that the purchaser furnish Shell with monthly statements showing how much gas was received under the contract and the amount owing therefor to Shell (R. 18, 90).

[4] This increase was admittedly authorized under Shell's contract and is not at issue here. It has been suspended and its justness and reasonableness is pending before the Commission in another proceeding under §4(e) of the Gas Act.

The Commission accepted the filing of the Shell contract and simultaneously fixed the matter for hearing "for the purpose of determining and fixing the rate properly effective on June 7, 1954" (R. 110-111). Texas Gas, present purchaser under the Shell contract, and Louisville Gas & Electric Company, a customer of Texas Gas (petitioners in No. 167), were permitted to intervene and, together with Commission Staff Counsel, participated in the hearing which was held on April 29, 1957.

(b) Decision of the Presiding Examiner.

The Presiding Examiner decided that the February 1954 agreement between the pipe line and Atlantic was a contract for the purchase of gas within the meaning of and hence activated the Shell clause (R. 112-126).

(c) Order of the Commission.

On exceptions the Commission reversed the Examiner and held that Shell's effective June 7, 1954 price was 8.997¢ per Mcf (R. 126-137). Shell applied for rehearing which the Commission denied (R. 143-150).

(d) Opinion of the Court of Appeals.

The Court held that the February 17, 1954 agreement constituted entry by the pipe line into a contract which activated the Shell clause. The Court vacated the Commission's order and remanded for determination of whether the price in the February, 1954 contract was indeed higher than the Shell price. The Court did not find it necessary to pass on the issue of whether the 1943 Atlantic contract created a binding and enforceable obligation as to each of the last four five-year periods (R. 164-165), this being one of the issues extensively briefed and argued to the Court.

(e) The Facts.

The 1951 Shell-Louisiana contract contains the following provision ("Shell clause") (R. 66-67):

> **"If at any time after December 31, 1951, Buyer shall enter into a contract providing for the purchase by it of gas produced from a field or fields located, and delivered to Buyer, within a radius of fifty (50) miles of any point of delivery provided hereunder, Buyer shall forthwith notify Seller of such fact, and if the price per one thousand (1000) cubic feet at any time payable under such other contract is higher than the price payable hereunder, each price payable hereunder which is less than the price payable at the same time under such other contract shall be immediately increased so that it will equal the price payable under such other contract. In determining whether the price payable under such other contract is "higher" than the price payable for gas under this contract, due consideration shall be given to the provisions of this contract as compared with such other contract as to quality of gas, delivery pressures, gathering and compressing arrangements, quantity, provisions regarding measurement of gas, including deviation from Boyle's Law, taxes payable on or in respect of gas delivered and all other pertinent factors."**

Prior to the Shell contract, Atlantic, as seller, had entered into a "Gas Purchase Contract" with Defense Plant Corporation, as buyer, dated September 1, 1943 covering the sale of gas in the North Tepetate Field,[5] Acadia Parish, Louisiana (R. 81-96) ("1943 Atlantic contract"). In this contract, which provides that the "*rights of the parties*" are to continue for the producing life of the field but not to exceed 25 years (R. 90-91), the "*Seller agrees to sell*" and "*Buyer agrees to buy*" specified *daily* quantities of gas to be delivered in the field where the gas is produced (R. 82, 83-84).[6] The contract fixes a definite

[5] This field is within the 50-mile radius of the delivery point [illegible] (R. 15).

price for the first five years (R. 85-86), but no price is fixed subsequent to the first five years. Rather, the contract provides (R. 86):

> "(b) At the end of the first five-year period, Buyer and Seller are to reach an agreement as to the price for gas sold and delivered under this contract during the second five-year period. The price to be paid during such second five-year period is to be agreed upon at the beginning of such period after a survey of prevailing prices for gas being sold in similar quantities in the southwestern part of Louisiana.
>
> "(c) During succeeding five-year periods, prices to be paid will be determined at the beginning of each period in the same manner as provided for in paragraph (b) above.
>
> "(d) In the event that the parties are unable to agree upon the price to be paid for gas after the first five-year period, in accordance with the arrangements set forth in paragraphs (b) and (c) above, such determination shall be submitted to arbitration in accordance with Condition XII."[7]

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[7] Condition XII reads (R. 91-92):

> "• • • The party desiring such arbitration shall notify the other and in such notice shall name an arbitrator, the arbitrator to be appointed by the other party shall be named within ten (10) days after receipt of such notice of arbitration, and an additional arbitrator shall, within ten (10) days of the appointment of the second arbitrator, be selected by the two (2) arbitrators theretofore appointed, but if one of said parties shall have failed to appoint an arbitrator within the time provided herein, it is expressly understood and agreed that the sole arbitrator shall arbitrate the question alone. If arbitrators shall have been appointed by the respective parties and shall have failed to select the third arbitrator within the above stated time, the third arbitrator shall be appointed by the senior Judge of the 5th Federal Judicial Circuit upon application therefor by either of said parties to the arbitration.
>
> "• • • The decision in writing signed by a majority of the arbitrators shall be final and conclusive with respect to the matter submitted and the parties hereto agree to accept and abide by the same."

War Assets Administration succeeded to the rights and obligations of Defense Plant Corporation as purchaser under the 1943 Atlantic contract, and by letter agreement between War Assets Administration and Atlantic dated October 26, 1948, those parties agreed upon a price for the six-month period from September 1, 1948 to March 1, 1949 (R. 96-97). This agreement provides that at the end of that six-month period the parties "*will negotiate*, in accordance with paragraph III b and d, the price to be paid for gas delivered during the remaining four years and six months of the second five-year period as provided in the contract" (R. 97).

Pursuant to the foregoing agreement to negotiate, Atlantic and Reconstruction Finance Corporation (then successor to Defense Plant Corporation) entered into a contract dated February 16, 1949 (R. 99-104). This contract provides in part (R. 100):

> "Whereas, the [1943 Atlantic contract] provides . . . that at the end of the first five-year period the Buyer and Seller shall reach an agreement as to the price for gas sold and delivered under this contract to be effective during the second five year period; and
>
> "Whereas . . . ; and
>
> "Whereas, *an agreement was reached* between Buyer and Seller *as to the purchase price* for the period [to March 1, 1949] . . . , and it is desired by the parties hereto that a *new agreement* be reached as to the price to be effective during the remainder of the second five year period of the contract."

The contract of February 16, 1949 (R. 99-104), in addition to amending certain quantity provisions of the previous contract of September 1, 1943, provides (R. 100):

> "Paragraph III of the said contract of September 1, 1943, is hereby amended to provide that, for

> the period beginning March 1, 1949, *and ending August 31, 1953,* the price for gas shall be five cents (5¢) net per one thousand (1,000) cubic feet. . . ."

On May 11, 1949 the pipe line (Louisiana) succeeded to the rights and obligations as purchaser of the North Tepetate gas from Atlantic (R. 105). On August 27, 1953, the pipe line wrote to Atlantic advising that the "price provisions [of the prior amendments to the 1943 Atlantic contract] expire on August 31, 1953" and evidenced willingness "to commence negotiations with you concerning such price" (R. 36-37). Pursuant to this request and starting in September, 1953, negotiations took place looking toward agreement on price between Atlantic and the pipe line. At least four meetings were held and there were numerous telephone conversations, with negotiations lasting over a period of approximately 5½ months (R. 25), and finally culminating in a written contract between Atlantic and the pipe line dated February 17, 1954 (R. 46).

Participating in the negotiations were W. L. Bowser (a witness at the hearing) and other parties representing Atlantic; and B. C. Adams, Jr., Vice President, and H. L. Mann, Vice President, together with other parties representing the pipe line (R. 21). The parties had difficulty coming to agreement; Atlantic contended for about 16¢ per Mcf, while the pipe line contended for 8.99¢ per Mcf (R. 23, 25). Mr. Bowser of Atlantic who negotiated both the 1943 and the 1954 contracts (R. 19-20, 21), and whose testimony was not disputed, testified that the contract did not specify a workable formula (R. 24-25) and that after many meetings and prolonged negotiations (R. 25):

> ". . . we finally haggled back and forth . . . they said, 'This is as high as we are going', and we said,

› can get that agreed to'. And
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cation and the aforesaid con-
ntic Refining Company was
Natural Gas Corporation.
ith Paragraph III of said con-
reed that the price to be paid
Gas Corporation to The Atlan-
y for gas sold and delivered
between September 1, 1953, and
h inclusive, shall be 12.2 cents
bic feet at a pressure base of
received at the central point
n the original contract, regard-
gas is delivered to a government
addition, Buyer shall reimburse
severance taxes, or similar taxes,
gated to pay and has paid to the
on such gas."

The agreement was "Agreed to and Accepted this 22nd day of February, 1954" by the pipe line (R. 47). On the same date, H. L. Mann, Vice President of the pipe line who participated in negotiating the contract and who executed it in behalf of the pipe line, returned the document to Atlantic with a letter reading in part as follows (R. 47-48):

> "* * * we are enclosing * * * letter *agreement* dated February 17, 1954, *covering the sale of gas,* * * *."

Summary of Argument.

A. Our position on the question of judicial review is briefly this:

When, as here, an administrative agency decides a question of law on the basis of court decisions, and not on the basis of administrative expertise, the correctness of its determination is fully and independently reviewable by the courts. Particularly is that true in this case because in the regulatory framework of the Natural Gas Act as construed in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U. S. 332 (1956), the Commission had no power to establish the initial relationship between the parties. That relationship was established by the parties in a privately negotiated contract. The Commission merely undertook the simple task of construing the non-technical language which the parties used. It did so to determine what contract price the parties had made for themselves as of June 7, 1954.

The Commission's task was twofold: (1) to construe a non-technically worded clause in a privately negotiated contract (the Shell clause) and (2) to resolve whether an undisputed set of facts (the negotiations leading up to and the making of the February 1954 agreement) consti-

tuted entry into a contract as provided for in the Shell clause. The resolution of such questions is typical of the everyday business of courts, and on the basis of comparative qualification it would seem that the Court would be better equipped than the Commission to resolve them. Therefore, unless the issues somehow required and were decided by the Commission on the basis of specialized administrative competence, the Court of Appeals was fully empowered to determine for itself whether the issues had been correctly resolved.

We shall demonstrate that no unique administrative attribute was called for or invoked by the Commission. The issues lent themselves only to judicial resolution, and the case was tried and decided on that basis. The words in the Shell clause were used in their ordinary sense, hence the construction of the clause involved solely a question of law. *Great Northern R. Co.* v. *Merchants Elevator Co.*, 259 U. S. 285 (1922); *Brown & Sons Lumber Co.* v. *Louisville & Nashville R. Co.*, 299 U. S. 393 (1937). See also *Federal Maritime Board* v. *Isbrandtsen Co.*, 356 U. S. 481 (1958).[8]

B. The Commission did not base its determination on administrative expertise, industry usage, economic impact, or technical wording of the favored-nation clause, nor on any other administrative attribute. The Commission had no hand in formulating the Shell contract. The pertinent

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[8] *United Gas Pipe Line Co.* v. *Memphis Light, Gas & Water Div.*, 358 U. S. 103 (1958) does not control this case. As we understand *Memphis*, the Commission had construed a provision in a pipe line service agreement which adhered closely to the Commission's Order 144, thus in effect construing its own language. In *Memphis*, this Court said (358 U. S. at 114): "It seems sufficient to say that the record shows that these agreements are typical of the 'tariff-and-service' arrangements contemplated by the Commission Order No. 144. . . ."

facts are clear. There was no weighing of cost allocation factors, as justness and reasonableness of the price was not involved; nor was there any question of whether the price was in the public convenience and necessity.[9] Industry usage with respect to favored-nation clauses was not raised at the hearing or relied on by the Commission as a basis of its determination, nor was any evidence introduced in that regard. No peculiarly administrative consideration went into the making of the contract or into the resolution of the issue. In brief, the question was purely judicial in nature, not administrative.[10] See *United States* v. *Western Pacific Railroad Company*, 352 U. S. 59 (1956); *United States* v. *Chesapeake & Ohio R. Co.*, 352 U. S. 77 (1956).

When, as here, the administrative agency purports to resolve a question on the basis of legal reasoning and judicial precedents, and the issue does not call for nor does the agency invoke any essentially administrative function, the correctness of its conclusion must be judged on the basis of the reasoning it invokes. *SEC* v. *Chenery Corp.*, 318 U. S. 80 (1943). Especially should that be true, we submit, when as in this instance the issue resolved is one which the statute does not expressly authorize the agency to resolve, let alone require it to do so.

Nor do considerations of uniformity enter into this case. Uniformity in the construction of contracts, where the question is one of law as here, ". . . may ultimately be

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[9] On June 4, 1956, prior to the hearing, the Commission had issued an unconditional certificate of public convenience and necessity to Shell authorizing it to continue this sale. *In the Matter of Shell Oil Company*, Docket No. G-5035.

[10] In his brief for the Examiner, the Commission Staff Counsel even contended that the proceeding should be dismissed "in respect of the contract interpretation question" *as it was so judicial in nature the Commission had no power to resolve that question* (R. 113-114, fn. 2).

reviewed by [the Supreme] court . . . and thereby uniformity of construction may be secured." *Great Northern Rwy. Co.* v. *Merchants Elevator Co.*, 259 U. S. 285 at 290-291.[11]

The Commission resolved, solely on the basis of its concept of judicial doctrine, what was essentially a private dispute between Shell and the pipe line. Had those parties agreed on the June 7, 1954 price, the Commission would have undoubtedly accepted their figure as Shell's initial regulated price, and there would have been no hearing. The fact that, as a general proposition, an administrative agency might be endowed with a specialized competence to resolve some issues coming before it, does not mean that every issue which it resolves either calls for or gets such consideration. And unless it does—as the present issue did not—the agency's determination is fully reviewable by the courts on the basis of correctness. Otherwise, administrative expertise—even latent expertise—would be a controlling factor in itself.

C. Section 19(b) of the Natural Gas Act (App. A hereto) invests the Courts of Appeals with jurisdiction "to affirm, modify, or set aside [the Commission's] order in

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[11] See also: *Davies Warehouse Co.* v. *Bowles*, 321 U. S. 144 (1944) where the Court said (p. 156):

> "Lastly, it is contended that we should accept the Administrator's view in deference to administrative construction. The administrative ruling in this case was no sooner made than challenged. We cannot be certain how far it was determined by the considerations advanced, [including uniformity] mistakenly as we think, in its defense in this case. It has hardly seasoned or broadened into a settled administrative practice. If Congress had deemed it necessary or even appropriate that the Administrator's order should in effect be final in construing the scope of the national price-fixing policy, it would not have been at a loss for words to say so. We do not think it should overweigh the considerations we have set forth as to the proper construction of the statute."

whole or in part." While §19(b) is silent as to the court's review power with respect to Commission conclusions of law, it does provide that the "finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive." It further provides that the "judgment and decree of the court [of appeals], affirming, modifying or setting aside, in whole or in part, any such order of the Commission, shall be final," subject to review by this Court.

Section 19(b) clearly contemplates that there will be no limitation on the court's power to review for itself the Commission's conclusions of law. The specification of limitation on review as to Commission fact findings, together with the section's silence as to other Commission conclusions, makes this clear. Any doubt in that regard is resolved by §10(e) of the Administrative Procedure Act (App. B hereto) which, except so far as the statute precludes judicial review or agency action is by law committed to agency discretion (neither of which is present here), requires that "the reviewing court *shall decide all relevant questions of law . . .*"

Merchants Elevator (259 U. S. 285), *supra*, and *Brown & Sons Lumber* (299 U. S. 393), *supra*, hold that tariff construction "presents ordinarily a question of law which does not differ in character from those presented when the construction of any other document is in dispute", 259 U. S. at 291, and, *ibid.*, "When the words of an instrument are used in their ordinary meaning, their construction presents a question solely of law." The principle of those cases, together with the provisions of §19(b) of the Natural Gas Act and §10(e) of the Administrative Procedure Act, make clear that the Court of Appeals was empowered to determine for itself whether the Commission had *correctly* resolved the issue.

II.

The Court of Appeals correctly concluded that the Shell clause was activated by the February 17, 1954 agreement. The Commission (1) misread and improperly injected into the Shell clause language which the parties neither used nor intended, (2) erred as a matter of law in concluding that the February 17, 1954 agreement did not constitute entry into a contract, and (3) by its foregoing errors, largely defeated the purpose of the clause, thus completely distorting the agreement of the parties which they clearly expressed in their contract.

A. The Commission improperly injected language into the Shell clause. But what is even more serious, it went on to conclude that the February 1954 agreement was not a contract within its revised wording of the clause. The Commission construed the Shell clause to require a "new" contract (R. 130, 147). But the clause permits of no such interpolation. We have not challenged the Commission's power to determine what contractual price the parties fixed for themselves at a given date; we do challenge its right to create by construction a contract the parties neither made nor intended.[12]

The Commission did *not* conclude that the Shell clause required the pipe line to enter into a *new* contract covering a

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[12] Petitioners do not appear to deny that the *usual* objective of a favored nation price clause in a gas purchase contract is to give the seller a top price, as the court below correctly observed in passing. Rather they contend that there are *limitations* upon the general coverage of these clauses and that the *limitation* in this case excluded the February 1954 agreement (Govt. Br. pp. 31, 33-34, 44; Br. of Texas Gas and Louisville pp. 21, 27, 28). Since the Commission employed ordinary rules of construction it should have construed the *limitation* strictly, especially since it was prepared by the pipe line. The language of the Shell clause suggests no such limitation as the Commission and petitioners contend for. If such limitation is to be maintained it can only result from construction based upon the supposed but latent intention of the pipe line to establish an exception of which its own words give no hint.

new supply of gas, as petitioners appear to view its order and as they contend the clause requires.[13] Had the Commission so construed the Shell clause it would have disposed of the matter in a sentence or two because obviously the February, 1954 agreement is not a *new gas supply contract.* But the Commission concluded that the February, 1954 contract was not a "new" contract but was merely action taken under a pre-existing contract. The Commission comes to this conclusion by reasoning that the 1943 Atlantic contract contained an arbitration clause which caused it to continue as a binding contract (R. 132, 147).

It therefore seems apparent that the Commission would have held the Shell price to have escalated if the 1943 Atlantic contract *had not contained the arbitration clause,* but had contained only the agreement-to-agree clause, because in that event the February 1954 agreement would have been a "new" contract within the Commission's reasoning, although it would not have covered a *new gas supply.* Thus it is evident that the Commission's conclusion turned on its version of the status of the February, 1954 agreement which it felt could not be another contract. The fallacy inherent in the Commission's reasoning is that an agreement cannot refer to a prior contract and at the same time itself be a contract. But there is no reason why that cannot be so. The principle is recognized in *American Colortype Co.* v. *Continental Colortype Co.*, 188 U. S. 104, 107 (1903) where the Court speaking through Mr. Justice Holmes said:

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[13] At p. 42 of the Government's Brief, it is said the Shell clause applies only when the buyer "enters into a *new gas-supply contract.*" At p. 44 they say the Shell price would escalate "only when the buyer thereafter entered into a *new supply contract.*" See also pp. 13, 40. The Brief of Texas Gas and Louisville (p. 28) speaks in terms of the "limitation" in the clause applying "if Texas Gas should enter into a *contract for the purchase of new gas. . . .*"

> "The allegations show that, having the old contract before them, the parties came together under a new agreement, which was determined by reference to the terms of that contract, but which none the less was personal and immediate."

B. The Commission's construction defeats one of the principal purposes of the Shell clause. The clause's obvious purpose is to give the seller equality of price treatment resulting from subsequently *negotiated* agreements pursuant to which the pipe line pays a higher price for gas from another producer. The Commission's construction wipes out that purpose by creating a void in the contractual pricing arrangement which the parties obviously did not intend to exist.

It seems apparent that Shell and the pipe line intended their contract to include a comprehensive pricing arrangement. Thus the contract contains its own fixed price step-up clause (R. 65) pursuant to which Shell gets its own bargained-for protection in that regard as against other existing contracts of the pipe line.[14] The Shell contract also contains a typical "price redetermination" clause,[15] but this clause cannot be invoked during the first ten years of the contract (R. 67-68). And the contract also contains the favored nation clause (R. 66-67) which is designed to fill whatever gap might otherwise exist, thus assuring to

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[14] We do not contend that the Shell clause covers future higher prices paid by the pipe line as the result of post-1951 fixed price step-ups taking place under pre-1952 contracts. As noted, Shell got its own bargain in that respect. Additionally, the pipe line's contract with Atlantic *does not* contain a fixed price step-up clause, hence there was no occasion for the pipe line to have prepared the clause to give Shell price equality with Atlantic in that regard.

[15] Under this clause the parties, beginning January 1, 1962 and January 1, 1967, *redetermine* the contract price to equal the average of the three highest prices then being paid in a specified area, with the contract's then current price as a minimum (R. 67-68).

Shell equal higher price treatment which the pipe line might thereafter agree to pay under *negotiated* agreements.

Yet the Commission construed the Shell clause so as to carve into it a gap which the clause's language does not fairly admit of and which the parties obviously did not intend should exist. Shell and the royalty owners under its leases from which the gas is produced would be just as adversely affected by the pipe line paying a higher price under a newly *negotiated* agreement arising out of a pre-existing arrangement as they would by a higher price resulting from the pipe line entering into a contract covering a new supply of gas. And that, of course, is why the clause merely calls for entry into "*a contract*" for the purchase of gas at a higher price and is not limited to a new supply of gas, as it would have provided had that been the intention. It would, we submit, be a distortion of the basic concept and purpose of the clause to permit its avoidance in the circumstances of this case by injecting into it, as the Commission did, a limitation which was significantly omitted.

C. Even if the Shell clause requires entry into a "new" contract, as the Commission erroneously held, the February 17, 1954 contract nonetheless fulfilled the clause.

The Commission reasoned that the February, 1954 agreement was not a "new" contract because it "merely represents action taken under a pre-existing contract" (R. 130). In this respect the Commission erroneously concluded that another contract cannot arise out of a pre-existing contractual relationship between the parties. That, of course, is not so. *American Colortype Co.* v. *Continental Colortype Co.*, 188 U. S. 104, *supra*.

The Court of Appeals properly read the Shell clause as it is written, and concluded that if the February 17, 1954 agreement was not an entering of a contract "we are

at a loss as to how it would be properly and legally characterized" (R. 164). If the February, 1954 agreement constituted entry into a contract, as it undoubtedly did, that was unquestionably a "new" contract for the simple reason that it existed for the first time. The negotiated agreement of February, 1954 established for the first time the contract price at which Atlantic would sell its gas and the pipe line would buy it for the five-year term beginning September 1, 1953. A negotiated agreement supplying the essential element of price at which a commodity is to be bought and sold for a fixed period of time, if it is a contract at all—as this one clearly was—is certainly a "new" contract.

Therefore, even though the Commission put "new" into the Shell clause, it still erred in concluding that the February, 1954 agreement did not meet the clause. Had the Commission construed the Shell clause to require entry by the pipe line into a purchase of new gas from new sources of supply (which it did not, but which petitioners now say the clause required—see fn. 13, p. 17, *supra*) it would of course have disposed of the matter very briefly. But the Commission did not do that, and the reason no doubt is that the Commission realized that the Shell clause could not be stretched to that extreme.

D. In any event, and for the foregoing reasons, the conclusion of the Commission was not reasonably supported and its order was properly vacated by the Court of Appeals. Having erroneously applied—or failed to apply—basic legal concepts and doctrine to a clear factual situation, there was no rational or reasonable basis to support the Commission's determination. Therefore, in any event, the judgment of the Court of Appeals should be affirmed.

Argument.

The hearing was convened by the Commission due to the fact that when the Shell contract was filed the buyer and seller were in dispute as to whether an increase had taken place.[16] The resolution of this private dispute necessitated construction of a price clause which called for entry by buyer into a contract providing for the purchase of gas at a higher price, in the light of the buyer's having subsequently entered into a *negotiated agreement* with another seller of gas pursuant to which the parties established the contract price for the term September 1, 1953 to August 31, 1958 (R. 46).

The Examiner held the Shell price was increased by the February 17, 1954 agreement (R. 112-126). He found that the Atlantic clause "is a provision for price *negotiation* for 5-year periods subsequent to the first 5-year period" (R. 119), and that "it is obvious, of course, that the [Atlantic] clause is *not* (emphasis in original) a 5-year periodic price escalation clause having fixed and agreed upon steps" (R. 124).

The Examiner went on to conclude (R. 123):

> "The escalation clause did *not* (emphasis in the original) require a complete *gas purchase contract*, . . . It merely required that the 'Buyer shall enter into a contract providing for the purchase by it of gas' etc. It did not require a new or different source of gas than Buyer had theretofore contracted for. It merely provided for 'gas produced from a field or fields located, and delivered to Buyer, within a

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[16] In the Commission's order for hearing it is provided (R. 111):

> "It further appears that the issue of Shell's rates and charges effective on June 7, 1954 . . . is the subject of proposed litigation between the parties to the contract."

> **radius of fifty (50) miles of any point of delivery provided hereunder . . .' . . . The language is clear enough to reveal the intent of the parties without resort to parole evidence or self-serving memoranda. To miss its plain meaning is to do violence to the generally accepted and reasonable meaning of the sequence of the words of the English language used. The simplest analysis reveals the heart of the matter. Shell sought to cause its selling price to rise to that called for by any other contract Buyer made for gas after an agreed date . . . if the gas was produced in the same general area of competition as agreed upon (50 miles). The language was evidently broad; not narrowly technical in character."**

The Commission reversed its Examiner. The Court of Appeals vacated the Commission's order (R. 160-165).

Petitioners argue that the Commission reached its conclusion on the basis of its expertise and intimate knowledge of the industry's understanding of the meaning of different types of favored nation clauses; and that the Shell clause was worded as it is for the economic benefit of the pipe line. But petitioners do not point out wherein the Commission brought any of these factors into play, nor where there was any evidence to support them. Surely the Commission's belated reference to the other Shell contracts in its order denying rehearing cannot have that all-inclusive effect.

I.

On review of the Commission's order the court below was fully empowered to decide for itself whether the Commission had correctly resolved the issue.

A. The Commission resolved a question solely of law.

In reaching its conclusion the Commission did not purport to draw or rely upon specialized competence, expertise or other administrative specialty; nor did it consider or base its conclusion upon industry practice or economic impact; nor would the evidence in this record support any such conclusion. Since the matter at issue required only the construction of words used in an ordinary, non-technical sense in a privately negotiated contract, together with the determination of whether a given set of facts constituted entry into a contract, there was no occasion for the invocation of administrative expertise, industry practice, or economic impact; and the Commission did not invoke any of them.

We do not contend that every Commission order which resolves a question which might qualify as one of "law" rather than "fact", is fully judicially reviewable on the basis of correctness rather than reasonableness. We recognize that there may be instances where the issue, though classifiable as one of "law", is so intertwined with some underlying administrative consideration that the agency's determination should not be set aside if reasonably supported. But that is not this case. Here the Commission merely construed the ordinary words of a contract as it supposed a court would have construed them. In our view, it would be unreasonable to say that when an agency conclusion is based upon its version of court-established principles, the courts themselves who establish those principles

cannot inquire into the correctness of the agency's conclusion based upon them.

This case, we submit, is within the principle of this Court's decisions in *Great Northern R. Co.* v. *Merchants Elevator Co.*, 259 U. S. 285, *supra*, and *Brown & Sons Lumber Co.* v. *Louisville & Nashville R. Co.*, 299 U. S. 393, *supra*, the latter of which involved an order of the Interstate Commerce Commission, with suit having been filed in a federal district court on the basis of the Commission's order construing its "Jones" or "Combination Rule" which was applicable to the carriers' tariffs, and which dealt with permissible increases in rates on certain routes. This Court said, 299 U. S. at 397:

> "The shippers made reclamation, on the ground that the Combination Rule applies in every case where no joint through rate has been published over the route selected for movement. The Commission sustained the shippers' claim."

In differing with the Commission and affirming the Court of Appeals, it was held (299 U. S. at 397):

> "The rule declares that the prescribed formula is to be applied 'where no published through rates are in effect from point of origin to destination.' The language used is not technical. The meaning of the words is clear. There is no ambiguity. *The construction of these railroad tariffs presents, therefore, a question of law, not differing in character from those presented when the construction of any other document is in dispute. Great Northern R. Co.* v. *Merchants Elevator Co.*, 259 U. S. 285, 291, 66 L. ed. 943, 946, 42 S. Ct. 477. As, in each instance, there was available some through route from point of origin to destination for which joint through rates had been published, the rule, by its terms has no application.

We so hold despite the construction given to the rule by the Commission.

"The shippers contend that the construction given to the rule by the Commission is conclusive, because preliminary resort to the Commission was necessary [citations]. They argue that such preliminary resort was necessary, since the interpretation and application of the rule involved (a) the exercise of sound administrative discretion as to technical and intricate matters of tariff application and the relation of tariffs one to another; (b) the reasonableness of a practice of routing as between higher and lower-rated routes, and (c) uniformity in the application of rates, which is the paramount purpose of the Interstate Commerce Act. ***But the argument is not sound.*** To determine whether the rule was applicable to the several shipments does not call for, or indeed permit, the consideration of any of these matters. ***The simple question for decision, as to each shipment, is whether there existed 'published through rates' 'in effect from point of origin to destination.' The determination of that question requires ordinarily merely the examination of the tariffs. The enquiry would, in all respects, be like that commonly made by courts when called upon to construe and apply any other document*** * * * ***Here, the shippers might have brought their action at law without resort to the Commission."***[17]

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[17] See also *Phillips Petroleum Company* v. *Federal Power Commission*, 10 Cir., 227 F. 2d 470, cert. den. 350 U. S. 1005, *sub. nom. Michigan Wisconsin Pipe Line Co.* v. *Phillips Petroleum Company*, where, on review of a Commission order interpreting its own regulations and a gas purchase contract, the Court reversed the Commission, holding (227 F. 2d at 476):

> "We hold, therefore, that the [Commission's] orders of October 1st and December 8th were timely; that they were subject to review under Section 19(b) *as presenting purely questions of law involving the construction of a contract.* . . ."

Later decisions do not detract from *Brown & Sons* and *Merchants Elevator;* the latter, in fact, being referred to in *United States* v. *Western Pacific R. Co.,* 352 U. S. 59, *supra,* with the observation that (352 U. S. at 65-66): "There the Court held that where the question is simply one of construction the courts may pass on it as an issue 'solely of law.' " In *Western Pacific,* the Court also said (352 U. S. at 69):

> "By no means do we imply that matters of tariff construction are never cognizable in the courts. We adhere to the distinctions laid down in Great Northern R. Co. *v.* Merchants Elevator Co. (U. S.) *supra,* which call for decision based on the particular facts of each case. . . . We say merely that where, as here, the problem of cost-allocation is relevant, and where therefore the questions of construction and reasonableness are so intertwined that the same factors are determinative on both issues, then it is the Commission which must first pass on them."

We are not here concerned, as in *Western Pacific,* with the doctrine of primary jurisdiction, although we concede the interrelationship of some of the principles between primary jurisdiction and judicial review.[18] Here, the Commission passed on the issue. Actually, its view of the matter goes to confirm that we have here none of the factors which might have motivated a court to refer the issue to the agency for primary consideration had it gone to a court in the first place. We do not contend that the Commission did not have jurisdiction. Nor do we now urge that had the issue first gone to a court it could not properly have been referred to the Commission for its primary

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[18] See 4 Davis, *Administrative Law Treatise,* §30.09, p. 242, fn. 7 (1958).

consideration,[19] although that is a matter of some doubt. Our position is that, having gone first to the decisional level before the Commission and having been treated there in no light other than a court would have treated the question, the reviewing court is authorized to decide the question for itself.[20]

That appears to be within the general area of the result reached in the litigation involving the validity of the dual-rate systems of shipping conferences culminating in *Federal Maritime Board* v. *Isbrandtsen Co.*, 356 U. S. 481 (1958), involving court review of a Maritime Board order approving under the Shipping Act a dual-rate system of a shipping conference. The Court recognized the propriety of the divi-

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[19] In *Southwestern Sugar and Molasses Co.* v. *River Terminals Corp.*, 360 U. S. 411, 420 (1959) the question of the validity of an exculpatory clause in a towboat's tariff on file with I. C. C. was held referable to the Commission, but the Court assumed that the question was "one appropriate ultimately for judicial rather than administrative resolution."

[20] See also *Phillips Petroleum Co.* v. *Wisconsin*, 347 U. S. 672, *supra*, in which the Court said (347 U. S. at pp. 677-678):

> "The Commission found that Phillips' sales are part of the production and gathering process, or are 'at least an exempt incident thereof.' This determination appears to have been based primarily on the Commission's reading of legislative history and its interpretation of certain decisions of this Court. Also, there is some testimony in the record to the effect that the meaning of 'gathering' commonly accepted in the natural-gas industry comprehends the sales incident to the physical activity of collecting and processing the gas. Petitioners contend that the Commission's finding has a reasonable basis in law and is supported by substantial evidence of record and therefore should be accepted by the courts, particularly since the Commission has 'consistently' interpreted the Act as not conferring jurisdiction over companies such as Phillips. See Gray v. Powell, 314 US 402, 86 L ed 301, 62 S Ct 326; N. L. R. B. v. Hearst Publications, Inc. 322 US 111, 88 L ed 1170, 64 S Ct 851. We are of the opinion, however, that the finding is without adequate basis in law, and that production and gathering, in the sense that those terms are used in § 1 (b), end before the sales by Phillips occur."

sion of functions between court and agency under which the latter "makes a preliminary comprehensive investigation of all facts, analyzes them, and applies to them a statutory scheme as it is construed" (356 U. S. at 498). Thus the employment of the primary jurisdiction doctrine is "to prepare the way, if litigation should take its ultimate course, *for a more informed and precise determination by the Court* of the scope and meaning of the statute as applied to those particular circumstances" (356 U. S. at 498-499).

In this case there was no question of reasonableness of the rate; no problem of cost-allocation or other factor inherent in the determination of reasonable rates; and no question of natural gas policy, or of industry practice or the economic impact of favored nation clauses. The sole question was *what was* the effective contract price at a given date under a privately negotiated contract, not whether it was a lawful or reasonable price. Thus the Commission decided a question solely of law, and under the principle of the foregoing cases its conclusion was fully reviewable as to its correctness.

B. The Commission did not resolve the issue on the basis of expertise, industry practice, or economic impact, nor did the issue permit such determination.

The Commission resolved the issue solely on its conception of judicial doctrine. Not a single reference is made by the Commission to any technical or special word, phrase or circumstance which even tends to tint the issue with uniqueness. Nothing is said of the economic impact of different kinds of price increase clauses. Not a word is mentioned about industry understanding or usage.[21] Nor is there a

[21] The Commission's belated reference in its order denying rehearing to a selected few other contracts entered into by Shell

single word of testimony in the record dealing with any of these factors, and we deny that any industry understanding exists as to various "types" of favored nation clauses.

On the contrary, the Commission's original order (R. 126-137) and its order denying rehearing (R. 143-150) show undeniably that the Commission gave no consideration to specialized know-how or industry practice or economic impact. The Commission relied upon court decisions and legal texts as the sole basis for its conclusion. The following makes this clear:

(1) After concluding that the effective price was determined by the amount of money changing hands on June 7, 1954 rather than by the contract price (R. 129), the Commission, "as an alternative ground" determined that the price had not increased, because (R. 130):

> "The agreement with Atlantic does not constitute a *new* contract as required by Shell's escalation clause, but merely represents action taken under a pre-existing contract between Texas Gas and Atlantic."

(2) Noting that *"Shell's contract was prepared by Texas Gas"* (R. 130), and that the arbitration clause in the Atlantic contract "makes it clear that where the parties are unable to agree arbitration of the price dispute is assured" (R. 131), the Commission states the question thus (R. 132):

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with other pipe lines was not for the purpose of indicating *industry understanding* of the meaning of differently worded favored-nation clauses. The other contracts were those of Shell only and did not include any other producers. When he was permitted to introduce these other contracts in evidence despite objection by Shell's counsel, the attorney for the pipe line stated that they were competent to show "difference in the language of the clauses and *infer* therefrom a difference in the meaning of what shall be done thereunder" (R. 29). Thus the contracts were not even introduced for the purpose of showing industry usage.

> "The question before us is whether the letter agreement constitutes a *new* contract for the purchase of gas or whether it merely represents action taken pursuant to the pre-existing 1943 Atlantic contract."

(3) After stating that (R. 132) "We believe the latter is the correct view," and saying that its conclusion made it unnecessary to consider whether the Atlantic contract contained a "certain enough" standard to extend the contract after the first five-year period because "paragraph (d) provides for a definite method by which a price will be fixed in case the parties fail to agree" (R. 132), the Commission devotes the rest of its order attempting to justify its conclusion on judicial doctrine, and starts out by saying (R. 132):

> "*The cases show* that a contract will not fail for want of certainty where a future price is to be fixed by arbitrators or other third parties (citations)."

After discussing the court cases, the Commission observes (R. 133):

> "*We do not think that any possible view as to the applicable state law alters this conclusion.*"[22]

Then follows a discussion of legal authorities including the Restatement of Conflict of Laws, the Uniform Sales Act, and certain Articles of the Louisiana Civil Code and cases decided by the Louisiana courts, including what we believe to be a misinterpretation of a French commentator's views (R. 133, 134), with the conclusion (R. 134):

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[22] One of the legal issues before the Commission (and the Court of Appeals) was what law governed validity and enforeability of the Atlantic contract. We have always contended that Louisiana law, the place of performance, governed, but that is a part of the issue which the Court of Appeals felt unnecessary to pass on.

> "*Because the questions of law here involved* have been adequately briefed before the presiding examiner we do not believe any purpose would be served by holding oral argument as requested by Shell."

In the concurring statement by one of the Commissioners, he observes that (R. 136) "The primary responsibility for the interpretation of the *legal effect* of tariff or rate schedules filed by regulated companies vests in the regulatory agency with whom they are filed."[23] The Commissioner goes on to state that the interpretation of the contract "in its capacity as a rate schedule" is the Commission's responsibility and "to the extent that the discharge of this responsibility requires the interpretation of the legal effect of a given set of facts in the light of its terms and conditions, we have the right and the duty to do so." (R. 136-137).

Since the so-called "rate schedule" was nothing more than a privately negotiated contract entered into several years before the Commission assumed jurisdiction, and since natural gas companies are free to make private contracts (*United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U. S. 332, *supra*), and since the Commission set

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[23] The Commissioner says that preliminary resort to the Commission is required "*because* the inquiry is essentially one of fact and of discretion in technical matters" (R. 136). We submit that preliminary resort to an administrative agency is not required *because* of those factors but only *when* the inquiry is such. The Commission instituted this proceeding not for the reasons stated by the concurring Commissioner, but because Shell subsequently filed an increased rate which was suspended and the Commission felt it "would, of course, be necessary in connection with any rate proceeding after suspension of increased rates, such as the proceeding actually instituted against Shell by our order issued March 13, 1957, in Docket No. G-12192, that we know the rate previously in effect both for the purposes of the proceeding and in computing refunds if it should turn out that the new rate, or part of it, was not justified" (R. 128).

out only to construe the contract to determine what price the parties had contractually fixed for themselves and thus settle a private dispute, it is difficult to see how the Commission could construe this "rate schedule" in any capacity other than a private contract.

In its order denying rehearing the Commission reiterates that the Shell price had not increased "although Texas Gas *had entered into a letter agreement for the purchase of gas* at 12.5 cents per Mcf . . . from The Atlantic Refining Company" (R. 144). The order on rehearing is concerned primarily with the circumstance that the Atlantic contract embodied a "contract to determine the price by arbitration, and this contract is not invalid . . ." (R. 146). After so concluding the Commission adds (R. 147):

> "*We may add at this point* that where Shell and its buyer did intend that escalations take place when prices were raised under either old or new contracts, language was used calculated to achieve this result, which may be compared with that used in Shell's contract with Texas Gas quoted in our previous order. *While we do not wish to be considered as interpreting such language here,* the contrast with the language used in Shell's contract with Texas Gas is significant."

This rather belated remark coming for the first time in the order denying rehearing can hardly be taken to have the overriding effect of transforming the Commission's judicial approach into an administrative one so that it would follow that the Commission reached its result on the basis of industry practice or understanding. As the Commission appears clearly to indicate, it referred to these other contracts not to show that each was exclusively representative

of a set industry pattern, but merely to show that by contrast in language in different contracts entered into by Shell, it felt that a different intent was indicated on the face of the language used in the instant contract.

We submit that in this dictum the Commission again fell into error. These other contracts made with other pipe lines under different circumstances and in different producing fields have no relevancy in casting light on what was meant by the instant contract, especially when, as here, the record shows what was intended to be accomplished by the Shell clause (R. 13-14, 15). Additionally, a showing that some favored-nation clauses apply to *any* higher price paid by the pipe line does not help in solving this case; it only demonstrates that the *usual* clause is all-inclusive and any *limitation* thereon should be clearly expressed. If resort is to be had to other contracts to show what the instant clause meant, particularly as our clause was prepared by the pipe line, we submit that when pipe lines intend to limit the favored nation clause so that the price will escalate only when they enter into a subsequent contract covering a new supply of gas, they say so.

In hearings before the House Committee, 84th Cong. 1st Sess. on H. R. 4560 (Harris Bill), there was submitted to the Committee a sampling of favored nation clauses. The example of a "Two-Party Favored Nation Clause" is reproduced at p. 689 of the Committee's Report of the hearings, and reads in pertinent part as follows:

> "3.(a) Buyer agrees that if, during the term of this contract it purchases from producers ***new gas from new sources of supply*** in the State of Louisiana south of a line . . . at a basic price schedule more favorable to Seller than that provided in this contract . . . Buyer shall thereupon notify Seller in writing of

such other purchase, submitting to Seller a copy of the new gas purchase contract . . .''[24]

The above example shows that when pipe lines want to limit favored nation clauses to future purchases of ''new sources of supply'', it is a simple matter to say so, and they do.

It is submitted that the Commission did not decide this case on the basis of administrative expertise, nor was there occasion for it to do so. It resolved the issues on its view of the law. Therefore, its order was fully reviewable.[25] *S. E. C.* v. *Chenery Corp.*, 318 U. S. 80, *supra*.[26]

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[24] In the Committee report on H. R. 6645, 84th Cong., 1st Sess. (House Report No. 992, 84th Cong., 1st Sess., p. 8), it is stated:

> ''According to testimony presented to the committee in the hearings, the various types of escalation clauses are principally the following:
>
> 1. The two-party favored nation clause: Under this clause the specified price in a long-term fixed contract is increased in the event the buying pipeline company shall pay a higher price to another producer for gas in the same field or in any area specified in the contract.''

It is noteworthy that, while the Committee describes the various types of escalation clauses, no mention is made of any so-called ''future'' type of favored nation clause.

[25] The Commission does not mention industry usage and we submit that none in fact exists. Every favored nation clause stands on its own wording. Had the Commission *sub silentio* assumed a usage to exist, it should have made known its assumption so Shell would have had an opportunity to show the contrary. Section 7 (d) of the Administrative Procedure Act (60 Stat. 241, 5 U S. C. §1006 (d)) would appear to make this necessary. That section provides in pertinent part:

> ''Where any agency decision rests on official notice of a material fact not appearing in the evidence in the record, any party shall on timely request be afforded an opportunity to show the contrary.''

And, ''whether usage exists is a question of fact'', Williston on Contracts (Rev. Ed.), Vol. 3, §662.

[26] See also *Federal Communications Commmission* v. *RCA Communications*, 346 U. S. 86, 91 (1953), where the Court stated:

> ''Since the Commission professed to dispose of the case merely upon its view of a principle which it derived from the statute and did not base its conclusion on matters within its own special competence, it is for us to determine what the governing principle is.''

C. Section 19 (b) of the Gas Act and §10 (e) of the Administrative Procedure Act make it clear that questions of law are fully and independently reviewable as to their correctness.

Section 10 (e) requires that the reviewing court "*shall* decide all relevant questions of law." (App. B. hereto). If we are right in our view that the Commission disposed of this case by resolving only a question of law, and if it be true that the question of contract interpretation in the instant circumstances was "relevant"—as we submit to be beyond doubt—then unless §10 (e) is to be completely disregarded, it seems to us that it fully empowered the court below to decide the question for itself.

While §19 (b) of the Gas Act does not specifically authorize the reviewing court to decide questions of law for itself, yet when that section is read in full and considered together with §10 (e) of the Administrative Procedure Act, it becomes apparent that the court is so empowered. If that is not so, and if on pure law questions the agency's determination is undisturbable if merely "reasonably supported", it would seem that the reviewing court's power under §19 (b) "to affirm, modify, or set aside the order in whole or in part" will be reduced to the mere chore of affirming the agency's order.

D. The Shell clause is not a patterned type but speaks for itself in clear ordinary language. The Commission's construction would defeat its purpose.

Petitioners, by emphasis of the expression "favored nation" clause, apparently attempt to create the impression that the Shell clause fits into one of a number of

special molds specifically designed to categorize all so-called "favored nation" price clauses used in the natural gas industry, and that the Shell clause fits snugly into the "future" type pigeonhole. They seem to feel that there are only two types of "favored nation" clauses, and no matter what a clause provides, nor what its obvious purpose is, the clause must be either what they choose to call a "future" type or an "old" type of clause. Petitioners would then have it that the Commission, fully aware of this practice, put the Shell clause into the "future" type category, hence the clause only applies when the pipeline enters into a *new supply* contract.

It is submitted that petitioners' position is wholly unfounded for these reasons:

1. The Commission did not consider industry practice or understanding in deciding this case, nor was it urged to do so, the reason no doubt being that there is no such industry practice or understanding relative to these clauses. Each clause means what it says—nothing more, nothing less. And it is not reasonable to believe the Commission was concerned with or acted upon industry practice or understanding in this case when it did not even mention any such practice or understanding.[27]

In this connection it is most significant that throughout its orders, and except for one occasion (R. 127), the Commission itself refers to the Shell clause not as a "favored nation" clause, but as an "*escalation*" clause. Thus, "The

[27] Expertise and industry practice were not urged upon the court below by any party. Additionally, §8 (b) of the Administrative Procedure Act, 60 Stat. 242, 5 U. S. C. 1007(b), requires that all decisions of administrative agencies "shall . . . include a statement of (1) findings and conclusions, *as well as the reasons or basis therefor*, upon all material issues of fact, law, or discretion presented on the record. . . ." If the Commission did base its conclusion on expertise or industry usage we are unable to find any such reason or basis in its order.

agreement with Atlantic does not constitute a new contract as required by Shell's *escalation* clause . . ." (R. 130), and ". . . within the geographical limitations of the [Shell] *escalation* clause . . ." (R. 131). See also: R. 144 line 8, 145 line 10; R. 147 line 10, where the Commission refers to the Shell clause as an *"escalation"* clause.[28] It is difficult to believe that if the Commission felt it was basing its conclusion on the Shell clause being what petitioners now call a *"future"* type *"favored nation"* clause, it would at least have referred to the clause as being a "favored nation" clause, rather than referring to it as an *"escalation"* clause, the latter of which could designate any type of price increase.

The Commission's failure to go into industry practice or understanding, or the economic impact of these clauses, is clearly understandable in view of the way in which this case was tried. No one contended that industry practice or understanding had anything to do with the case. It is true that the pipe line introduced some contracts between Shell and other parties. Each of those, however, was introduced for the purpose of showing that the other clauses applied to *any* higher prices paid by the pipeline irrespective of how the higher price was arrived at, so that a different intent could be *inferred* from the use of a differently worded clause (see fn. 21 pp. 28-29, *supra*). Not alone was there no evidence to show industry understanding about these clauses in general, but the fact of overriding importance is that there was no evidence whatsoever as to any industry

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[28] The clause is, we concede, one of a multitude which are generally referred to as "favored nation" clauses. We have no disagreement with the clause being called a "favored nation" clause. Our disagreement is with petitioners' pigeonholing it into their newly-created "future" or "new" type and then contending that that is what the Commission did, and how the industry considers the clause. We deny both.

practice or understanding *concerning the Shell clause*. And since *that* is the clause involved here, the absence of such evidence is fatal to petitioners' post-rationalization that industry practice and understanding were the predicate for the Commission's conclusion.[29]

An indication of how this case was tried to the Commission is the way in which the pipe line, Texas Gas, urged the matter upon the Examiner and the Commission. In its brief before the Examiner, Texas Gas referred to the Shell clause and urged (Answering Brief of Texas Gas, p. 8):

> "This is not a case where the parties have used some very technical terminology which has a special meaning so peculiar to the gas industry that no one else would understand it, or where there is shorthand or cryptic use of business terminology needing definition for the layman. In short, there is nothing puzzling about the escalation provision."

And in its Exceptions and Statement of Supporting Reasons filed with the Commission, Texas Gas refers to the Shell clause thus (p. 10):

> "The language here involved, however, is nonspecialized enough so that the average reader would

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[29] The following colloquy took place at the hearing concerning the admissibility of the other Shell contracts (R. 33-34):

> "Mr. Weston [Staff Counsel]: From the Staff point of view, I would make this point, that *there is no showing, certain, to date, of any trade practice in the formation of given categories of clauses into which the present controversy will fit, or any other controversy;* however, this does throw at least some light on the general subject."
>
> "Presiding Examiner: The situation in which the construction must take place.
>
> "Mr. Weston: Yes.
>
> "Presiding Examiner: While it doesn't necessarily tell you how to construe the words in the contract at issue here, *it does tell you you have to construe those words, not some other words, because there isn't any cut and dried pattern that it fits into. . . .*"

> easily grasp its meaning without indoctrination in trade usage."

Any doubt as to how the issue was treated by the Commission is completely dispelled by the Commission's petition for rehearing in the Court of Appeals. After observing that the Examiner did not rely on extrinsic evidence but decided the issue on the plain meaning of the Shell contract language, the Commission's petition states (pp. 3-4):

> "The Commission reversed the Examiner's holding on the Shell contract language, and concluded that *under the applicable law*, the Atlantic-Louisiana contract constituted a binding 25-year agreement and the February 1954 agreement constituted a step in the performance of that contract, not an independent five-year agreement . . . *Its decision rested explicitly on the contract language and did not incorporate any findings based on parol or extrinsic evidence, although such evidence was referred to in its order denying rehearing.*"

2. There is no general understanding in the industry that a clause such as the Shell clause is a "future" contract clause which applies only to a new supply contract. To construe the Shell clause that way would largely defeat its purpose. As shown at pp. 33-34, *supra*, when the intention is to restrict the clause's application to new supply contracts (as petitioners say was the case with the Shell clause), the contract so provides by stating: "Buyer agrees that if, during the term of this contract, *it purchases* from producers *new gas from new sources of supply*" the seller shall be entitled to the higher price. If, as petitioners contend, the Shell clause had been intended to apply only when the pipe line entered into a contract covering a new supply

of gas, it is hard to believe that an experienced pipe line would not have used language to express that intention when it prepared the clause.

There were only two witnesses at the hearing and they were called by Shell. The only testimony concerning the purpose of the clause was by Shell's witness Quinn who negotiated the contract, and he testified without challenge or dispute as follows (R. 13, 14):

> "Q. In the negotiations leading to the execution of this Shell-Louisiana Natural contract, what transpired relative to the price and particularly relative to the favored nations clause you have just identified? A. Well, of course, I might say that the two foremost considerations in this thing were term—we were asked for a 20-year term, which we hadn't done before.[30] And there came along with that, then, the price which would justify us in accepting a 20-year term at that time. At that time it was quite impossible to predict what gas prices would be down the line. *We were presented with this favored nation clause which we felt would protect us, at least would give to us the going price, the market price, as in years past in this operation.*
>
> "We had no other way, actually, to justify a 20-year contract."

At the time Shell and the pipe line entered into The 1951 Shell Contract (which rescinded and took the place

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[30] Petitioners appear to feel that by this remark the witness meant that Shell had not theretofore made a 20-year contract anywhere. We submit that the witness was referring to Shell's position with respect to its Chalkley gas which had theretofore been contracted to Defense Plant. The Court below appears to have so construed this testimony (R. 163). The negotiations about which the witness was speaking were those leading up to the Shell-Louisiana contract of May 1, 1951. That contract, it will be noted, refers to and rescinds the prior Shell contract covering this same gas (R. 57-58).

of a 1943 contract originally between Shell and Defense Plant, see R. 57-58) the pipe line (Louisiana) was then the purchaser under the neighboring Atlantic contract (R. 105). Therefore, the pipe line surely knew of the agreement-to-agree upon price clause in the Atlantic contract and knew that at five year intervals it would have to make an agreement with Atlantic on price. If there had been the slightest intent that future contracts fixing the new price under the Atlantic contract were not to activate the Shell clause, surely the pipe line would have said so when it prepared the latter.

The Article of the Shell contract dealing with "Prices" (Article VI, R. 65-68) makes clear that the parties intended a comprehensive pricing arrangement pursuant to which Shell would receive equal price treatment with other sellers to the pipe line in the same area. In this regard it is significant that the 1951 Shell contract contains (1) a fixed price step-up clause (R. 65); (2) a favored nation clause (R. 66-67); and (3) a "price redetermination" clause (R. 67-68), but this "price redetermination" clause does not become effective until January 1, 1962, more than ten years after the contract was made (R. 67).

It is noteworthy that the 1943 Atlantic contract does *not* contain a fixed price step-up clause. That being so, it was not necessary from the standpoint of the Atlantic contract for the pipe line to give Shell a favored nation clause so extensive as to protect Shell against *all* increases.[31] But the pricing arrangement as a whole, and particularly the wording of the Shell favored nation clause, show clearly that the parties intended that Shell would be

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[31] If in May 1951 Louisiana had any prior gas purchase contracts outstanding in the 50-mile radius of the Shell gas (none are shown in the record), Shell could protect itself by negotiating its own fixed step-ups, which it did as reflected by the step-up provision in its contract (R. 65).

protected against future *negotiated* agreements under which the pipe line agreed to pay a higher price to another producer. In no other way could Shell be treated on an equal basis.

The Government's brief actually demonstrates the reason why the Shell clause was intended to be operative in circumstances such as those presented in this case. In discussing the distinction between favored nation clauses from the seller's standpoint, the Government's brief states (pp. 35-36):

> "At the time of contracting, the seller can bargain directly for substantive concessions in its own contract similar to those in the buyer's existing contracts with other producers. Its claims for parity as against existing contracts can thus be directly negotiated and compromised, so that only the function of assuring equality with future contracts, *the terms of which cannot then be known, need be left to the 'favored-nation clause.'* "

That was precisely the function the Shell clause was designed and intended to fulfill, namely, equality with subsequent *negotiated* higher prices *which could not be known by Shell* at the time it entered into the 1951 contract. Shell and the pipe line could not possibly know in 1951 what price the pipe line and Atlantic would agree upon in the future under the Atlantic clause which called for them "to reach an agreement" and "price to be paid . . . is to be agreed upon . . ." (R. 86). It was that unknown and future-to-be-agreed-upon price which was left to the favored nation clause. The clause as drawn fulfills what would otherwise be a void in the comprehensive arrangement for price equality which was employed by the parties. The Commission's construction would create a serious gap

in this contractual arrangement and thus defeat one of the clearly intended purposes of the clause.

The language of the Shell clause suggests no such limitation as that the subsequent contract, to be a triggering one, must be a "new gas-supply contract" as the Government contends (Br. p. 42), or one "to acquire new gas" or "for the purchase of new gas" as petitioners in No. 167 contend (Br. p. 28). Language so readily handy to the pipe line would surely have been put in the clause had that been its intended purpose and had the pipe line not been in accord with Shell's understanding that the purpose of the clause was to ". . . protect us, at least would give to us the going price, the market price, as in years past in this operation" (Quinn, R. 14). But had the pipe line put language in the clause to limit it to the purchase of new supplies of gas, it is doubtful that it would have been acceptable to Shell because then it would not have given Shell the "going price" in the area. And "going price" or "market price" is just as effectively made by a higher price reached by way of an agreement-to-agree clause as by entry into a new contract covering a new supply of gas.

E. The Atlantic contract does not contain a price redetermination clause nor did the Commission so hold.

The purchaser in the 1943 Atlantic contract was "Defense Plant Corporation, a corporation created by Reconstruction Finance Corporation pursuant to Section 5d of the Reconstruction Finance Corporation Act . . ." (R. 81). This governmental agency was purchasing the gas "for the purpose of transporting gas to plants which have been or are being constructed in the vicinity of Lake Charles, Louisiana . . ." (R. 82). If, therefore, any industry

practice existed in 1943 under which *private pipe lines* required a long-term supply of gas to satisfy lending institutions who provide capital to finance construction of the lines and to satisfy the Commission in order to receive a certificate of public convenience and necessity, neither of those considerations was present here when Defense Plant Corporation bought the Atlantic gas to supply defense plants in the Lake Charles area during World War II.[32]

In the setting in which the contract was made, it is not surprising that while the *"rights of the parties"* were to continue for the life of the field but not beyond twenty-five years (R. 90-91), the parties saw fit to leave the price open for agreement at five-year intervals.

The 1943 Atlantic price agreement clause did not contain a definite formula for determining price as is the case in a price *"redetermination"* clause, nor did the Commission hold that the Atlantic clause was a price redetermination clause, nor could it properly have so held. Yet it seems that petitioners attempt to create an impression to the contrary, by referring to the February 17, 1954 agreement as "a mere price redetermination" (Govt. Br. 36, see also pp. 39, 42, 44, 45, 50, 51) and as "price adjustment by the parties" (Govt. Br. p. 46) and "price readjustment" (Govt. Br. p. 49, fn. 22). The petitioners in No. 167 appear to do much the same thing (Br. for Texas Gas and Louisville pp. 9, 10, 17, 20, 23).

The Atlantic price clause was not a price *increase* clause. It called specifically for *"agreement as to the price for gas"* (R. 86), thus requiring that the *contract price be created*

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[32] See p. 46 of the Government's brief where it speaks of the 1943 Atlantic contract as a long-term agreement with periodic price adjustments which it says accords with normal industry practice of employing long-term contracts.

by agreement. The contract did not contain a continuing price in the event agreement could not be reached. That, no doubt, is why the clause called for agreement *"at the beginning of such period"* (R. 86). In short, the Atlantic clause is not a "price redetermination" clause but merely a clause whereunder the parties agree that an entirely new and controlling contract price will be determined by agreement.

A typical price *"redetermination"* clause in gas contracts is a clause dealing *solely* with price *increases.* It contains a definite standard by which the *increase* is to be ascertained, using the average of the two or three highest prices being paid by interstate transporters in a designated area; and it leaves the then contract price as the continuing price if such average does not exceed it. The Shell contract, which is in the record, contains a typical price redetermination clause (R. 67-68), from which can be seen the complete dissimilarity between a "price redetermination" clause, and the Atlantic clause which calls for agreement as to price. The difference between the clauses is obvious. One, the price *redetermination* clause, calls for *increases,* gauged by a definite formula, to be calculated by simple arithmetic computation. The other, the Atlantic clause, is a unique and nondescript provision under which the contract price having completely expired, the parties *agree to agree upon the contract price* for a future term.

The nature of price redetermination clauses in gas contracts is recognized in legislation pending before Congress. H. R. 366, 86th Congress, 1st Session, §14(a)(3) defines the clause thus:

> "The 'better market clause' or 'price redetermination clause' under the terms of which the price

of the natural gas is or may be increased in the event the average of two or more prices which are paid by purchasers in a specified area is greater."[33]

II.

The Court of Appeals was correct in deciding that the February 17, 1954 agreement caused the Shell price to increase as that agreement was clearly entry into a contract by the pipe line.

A. The Decision of the Court Below.

The Commission read the Shell clause to require a new contract, and then went on to conclude that the February 1954 agreement was not a *new* contract but merely action taken pursuant to a pre-existing contract. The Court of Appeals (and the Examiner) read the clause as it is written and concluded that the February 1954 agreement constituted entry into a contract for the purchase of gas. "Actually," said the Court, "if the Louisiana-Atlantic agreement of February 17, 1954 was not an entering of a contract we are at a loss as to how it would be properly and legally characterized" (R. 164).

The Court observed that the Shell clause is *"one of the type"* of clauses commonly known as "favored nation" clauses and that the *"usual"* objective of favored nation clauses is to assure the seller a top price for its gas (R. 163). Petitioners seem to feel that, by this observation and its

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[33] In the Government's brief (p. 32, fn. 17) it is stated: "The 'price redetermination' clause provides for an *increased* price at periodic intervals based generally upon the average of the two or three highest prices being paid for gas in a defined area." This recognition by the Government should completely destroy any implication that Atlantic and the pipe line "redetermined" the price in accordance with a *price redetermination* clause.

observation that to make the February 17, 1954 agreement retroactive to the date of the original contract is "abstractly conceivable" but to do so would "take the law out of the realm of business practicalities" (R. 164), the Court overreached itself and trod upon exclusively administrative ground.[34]

We submit that is not so. When the Court's opinion is read as a whole it is clear that the Court was merely applying the usual rules of construction to the Shell clause, including what was obviously one of the main purposes of the clause. Since the construction of the clause, with its non-technical language, presented solely a question of law, the question remained one of law before the Court as it had been before the Commission. In resolving the law

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[34] Petitioners cite *Phillips Petroleum Co.* v. *F. P. C.*, 10 Cir., 227 F. 2d 470 (1955); cert. den. 350 U. S. 1005 (1956), to support the position that the February 1954 agreement was but performance of the 1943 agreement. The Court did say that certain letter agreements which spelled out the price which resulted from an escalator clause "were merely executory of the contract between the Parties" (p. 475). But that case involved not an agreement-to-agree clause as in the 1943 Atlantic contract, but rather an automatic price increase clause under which the price was to escalate in the same ratio as the pipe line's resale rate exceeded a stated price. The Court pointed out that (227 F. 2d at 472): "In accordance with the *'formula in the contract'* . . . the parties entered into a letter agreement. . . ." Also, at p. 475, the Court said: ". . . it is one thing to treat an escalated rate effective after June 7, 1954 as a change in rate or new schedule. It is quite another to treat a rate already in force on June 7, 1954 by virtue of the *automatic provisions of an escalator clause* in a contract as a new schedule or change in rates." And (p. 475): "But [the June 7, 1954 price] was nonetheless in force and effect and was being paid *not by force of letter agreements, but by force of the binding effect of the escalator clause which operated to fix the prescribed rate in accordance with the formula in the contract.*" It cannot here be said that after February 17, 1954 the price of 12.5¢ per MCF was being paid by virtue of any escalator clause in the Atlantic contract which fixed the price in accordance with a formula. Without the February 17, 1954 contract there was no price in the previous contract as the previous price expired on August 31, 1953 (R. 100).

question in construing the clause, the Court was therefore justified in applying the usual rules of construction, just as the Commission attempted to do. And in so doing, the Court merely looked to the purpose of the clause in the context of its use.

That the Court below was fully justified in doing so is supported by this Court's decision in *Santovincenzo* v. *Egan*, 284 U. S. 30 (1931). That case involved "the most favoured nation" clause (p. 35) in a treaty between the United States and Italy, and called for the construction of a clause in a treaty between the United States and Persia, which clause Italy contended it could benefit from by virtue of "the most favoured nation" clause in its treaty. In agreeing with Italy's construction this Court said (284 U. S. at 37):

> "In order to determine whether such a construction [of the Persia treaty] is admissible, regard should be had to the purpose of the Treaty and to the context of the provision in question."

The gist of the conclusion of the Court of Appeals is ". . . the fact cannot be avoided that, at least for purposes of the favored nation clause, the 'entering of a contract for the purchase of gas' has not been accomplished until the price has been established" (R. 164); and ". . . while there may have been enforceable means for settling the rate of payment in the event the parties could not agree, it would nonetheless be true that it was when the price was finally established, *by whatever means*,[35] that a contract had thereupon been entered" (R. 164).

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[35] The Government says (Br. p. 50) that the Court apparently recognized that "if the price had been fixed by arbitration, no new gas-purchase contract would have resulted." In view of this express statement by the Court, the Government's assumption appears unfounded.

By observing that it was "abstractly conceivable" to view the February 1954 contract retroactively, the Court, as we view it, was merely announcing that it had given full consideration to the Commission's views, and concedes that as an abstract proposition it is sometimes conceivable to view a contract to be retroactively effective. Thus, for some purposes, a contract to sell a commodity which is subject to a condition precedent (such as fixing of price) might, as a fiction, upon ripening into a sale when the condition is supplied, be said to be retroactive to the date of the contract to sell. But it would make an unreal thing of the law to employ that fiction in the circumstances of this case and thus largely defeat the intended purpose of the Shell favored nation clause.[36]

The Court correctly laid bare the Commission's erroneous legal conclusion that the February 17, 1954 agreement did not satisfy the Shell clause as it was not a "new" contract but "merely represents action taken under a pre-existing contract" (R. 130). The erroneous premise inherent in the Commission's conclusion is that the provisions of a previous agreement cannot be carried forward into a subsequent agreement, or, that parties once having agreed cannot thereafter agree. There is no legal or logical reason why a letter agreement executed in 1954 cannot refer to a prior agreement and at the same time itself constitute a contract. See *American Colortype Co.* v. *Continental Colortype Co.*, 188 U. S. 104, *supra*.

What was the legal relationship between Atlantic and the pipe line as of September 1, 1953? The time limit of their

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[36] There is nothing unseemly in a court noting "business practicalities" or "business realities". In *United Gas Pipe Line Co.* v. *Memphis, etc.*, 358 U. S. at 113, this Court said: "*Business reality* demands that natural gas companies should not be precluded by law from increasing the prices of their product. . . ."

previous price agreement ran out on August 31, 1953. If the parties could not agree on price, the matter of determining the price for them could be submitted to arbitrators provided one of the parties saw fit to invoke the arbitration procedure. But the parties saw fit not to resort to arbitration but rather to negotiate out their differences until they finally came to a meeting of the minds. Therefore, the question of what would have happened had they called upon arbitrators to fix the price for them is not material here. In concluding that the previous contract continued in force because it contained an arbitration clause, the Commission failed to give effect to the fact that the parties actually traded out their differences and entered into a contract. After top officials from the pipe line and Atlantic conducted extensive negotiations lasting over a period of about 5½ months (R. 25) and after having "haggled back and forth" (R. 25), they finally reached agreement and embodied their agreement in the contract of February 17, 1954. It is difficult to conceive of this agreement in any light other than entry into a contract providing for the purchase of gas by the pipe line at the new price. The end product of the negotiations—the February 17, 1954 agreement—was clearly a contract.

B. In any event the Commission's conclusion was not reasonably supported.

We have demonstrated, we believe, that the Court below was fully empowered to judge this case independently and to decide for itself whether the Commission's order was legally proper or legally erroneous. The Court, as we read its opinion, applied the usual rules of contract construction and decided that the Commission's order was legally erroneous. It may also be that by mentioning it to be "abstractly

conceivable" to make the February 17, 1954 agreement retroactive, the Court felt the Commission's conclusion was not reasonably supported. In our view it was not.

One of the basic errors of the Commission's conclusion is the assumption inherent in it that entry into a contract cannot result where an agreement grows out of a pre-existing contract. The Court of Appeals would not accept this fallacious premise; correctly laid it bare; and, with due recognition of the administrative function, remanded the case to the Commission to make the determination as to whether the Atlantic price was indeed higher than the Shell price. What the Commission failed to appreciate is that under the Shell clause it makes no difference whether the higher price results from a pre-existing arrangement or from an entirely new arrangement. The controlling factor is whether the higher price results from "ent[ry] into a contract . . .". Where a higher future price to the pipe line results *automatically* from an "old" contract, such as a fixed step-up increase under a pre-1952 contract, then we concede the Shell clause is not activated. But when the price previously paid by the pipe line under a pre-1952 gas purchase contract becomes higher than the Shell price, not by virtue of the *automatic* operation of a price escalation clause, but rather by virtue of the entry into another contract by the pipe line, then the Shell price clause is activated.

The Commission failed to recognize this distinction, although the Examiner and the Court of Appeals had no difficulty at all with it. The Commission seems to have assumed that in any instance that the pipe line had an outstanding pre-1952 contract in force, then, no matter how a price increase under such so-called "old" contract came

about, Shell could not benefit from the increase. This seems clearly to have been the Commission's approach from its statement concerning prices being raised under "either old or new contracts" (R. 147).

But the Commission's approach in this regard fails to take into account the wording of the Shell clause and the standard which the parties established in their contract. That standard called for the pipe line merely to enter into a contract after December 31, 1951 providing for the purchase of gas within the designated area at a price higher than the Shell price (R. 66-67). In essence, the controlling factor is not whether the activitating price is "raised under either old or new contracts" (R. 147) as the Commission erroneously assumes, but rather *the manner* in which the higher price comes into existence. If it results from the "ent[ry] into a contract" by the pipe line after December 31, 1951, the Shell clause is satisfied. And that, we submit, is precisely what the pipe line did when it entered into the February 17, 1954 agreement.

III.

Petitioners' post-rationalization of the Commission's decision is not supported by the record or the Commission's order.

A. Petitioners overweight the Commission's determination with expertise and industry practice and understanding. They would unduly limit the Shell clause on the unsupported basis that the pipe line's economics dictate that it must have driven a harder bargain with Shell than the clause provides, although neither the circumstances

attending the execution of the contract nor the words put into the clause can be stretched to that end. We deny that there is any industry understanding as to just what groove various types of so-called favored nation clauses fit into. Each stands upon its own wording. And aside from the fact that this case was not tried on the basis of industry practice or understanding, but rather as a straight contract interpretation case, the Commission itself did not purport to resolve the issue on the basis of administrative expertise or industry practice.

Petitioners stress heavily the fact that there were in the record certain other contracts entered into by Shell which contained favored nation price clauses pursuant to which the seller receives the benefit of *any* higher price paid by the buyer within a designated area; and that the Commission in its "we may add" observation on rehearing (R. 147) stated that "where Shell and its buyer did intend that escalations take place when prices were raised under either old or new contracts, language was used calculated to achieve this result, which may be compared with that used in Shell's contract with Texas Gas" (R. 147).

If the issue of the meaning of *the Shell clause* had revolved around industry practice or understanding, or had that even been collaterally considered, it is difficult to reconcile that fact with the fact that the record is utterly barren of evidence in that regard. Surely there would have been at least some evidence dealing with industry understanding *of the meaning of the Shell clause,* because after all, *it was the Shell clause* which was at issue, not some other clause such as those contained in the other contracts introduced in evidence by the pipe line and which concededly apply to *any* higher price paid by the buyer. Petitioners would now have the Court read the Shell clause as

if it applied only when the pipe line entered into a subsequent 30-odd page contract covering a new supply of gas. To support this position they point, not to any practice or understanding as to the effect that *the Shell clause here at issue* accomplishes that result (and we submit there is none), but rather to some other contracts which obviously cover *any* higher price paid by the pipe line. Hence, the net result of petitioners' position is that because there are some clauses which apply whenever the pipe line pays *any* higher price to another seller, whether resulting from a contract, a fixed step-up clause, or otherwise, it follows that *all other clauses* (including the Shell clause) apply only when the pipe line enters into a new contract covering a new supply of gas.

Had Shell urged in this case that its clause covered *all* higher prices paid by the pipe line, such as a fixed step-up resulting under a pre-1952 contract, then the other contracts might have some relevancy. But Shell has never made such contention. We concede the Shell clause does not apply to *all* higher prices paid by the pipe line. We contend, however, that it does apply when the higher price results from post-1951 entry into a *negotiated* agreement by the pipe line. It is for the foregoing reason that we submit the other contracts cast no light on intent in this instance. Actually, those contracts should never have come into evidence. But, at most, all they show is that on other occasions the parties made a different bargain. They do not establish that every other bargain should be construed to tilt to the other extreme.

Petitioners' position leaves no middle ground for favored nation clauses. Rather than each clause standing on its own wording, they would divide all clauses into two types. One extreme would cover every higher price. The

other extreme would only cover higher prices when the pipe line made a new contract covering a new supply of gas. There would be no in-between no matter what the consensual arrangement was. It would be anomalous to say, as petitioners in effect do, that because in some circumstances the parties to a gas purchase contract agree that the seller is to receive *all* higher prices the buyer pays to another, irrespective of how those higher prices come about, that in *all other* favored nation clauses in contracts made by that same seller, and no matter how another price clause is worded, the seller gets nothing unless the buyer pays a higher price under a new contract covering a new supply of gas. That approach would, we believe, compel gas sellers hereafter to insist that every favored nation clause be all-inclusive in its coverage.

We submit that contract rights should not be decided upon such a far fetched and erroneous assumption of industry practice as petitioners appear to assume exists. It was not proved; it was not alleged nor urged; it was not considered by the Examiner or the Commission; and in fact it does not exist. In the *Merchants Elevator* case this Court said (259 U. S. at 291-292):

> "When the words of a written instrument are used in their ordinary meaning, their construction presents a question solely of law. But words are used sometimes in a peculiar meaning. Then extrinsic evidence may be necessary to determine the meaning or words appearing in the document. This is true where technical words or phrases not commonly understood are employed. *Or extrinsic evidence may be necessary to establish a usage of trade or locality* which attaches provisions not expressed in the language of the instrument. Where such a situation

> arises, and the peculiar meaning of words, *or the existence of the usage, is proved by evidence,* the function of construction is necessarily preceded by the determination of the matter of fact."

B. Petitioners urge that Shell's action after learning of the February 1954 agreement indicates a limited construction of its clause. Neither the Commission nor the Court of Appeals appears to have given any effect to this contention, though it was made to each. At any rate, the following is significant:

The pipe line was required to "forthwith notify" Shell of its entry after December 31, 1951 into a contract providing for the purchase by it of gas (R. 67). This notice was never given with respect to the February 1954 agreement (R. 16, 35). In failing to give the required notice, the pipe line acted at its own risk. If it gave the matter any consideration at all, it may have felt that the 1954 contract did not activate the Shell price, although its own Vice President contemporaneously classified that contract as an *"agreement . . . covering the sale of gas"* (R. 47-48). No matter the reason, the fact remains that notice was not given, and this failure to comply with its notice obligation by the pipe line is the *sole* reason for Shell having to ferret out the details which should have been supplied by the pipe line. It is the cause of whatever delay there was on Shell's part.

After Shell accidentally learned of the 1954 agreement (R. 16), it had to gather the data (a copy of the 1943 Atlantic contract and a copy of the 1954 Atlantic contract) and consume the required time to support its position that it "had a new price coming up" (R. 16, 34). The evidence is clear that since learning of the February 1954 agreement, Shell has consistently adhered to its position that it was entitled to receive for its Chalkley gas the same price which

Atlantic received since September 1, 1953 for its gas sold under the February 1954 contract (R. 16-18).

Whatever Shell's delay in *communicating* its position to the pipe line, that delay is attributable solely to the pipe line's failure to comply with its obligation under the contract. The contract required no notice from Shell. The only requirement for notice called for the pipe line to notify Shell, and that notice was never given. Certainly a party cannot use its own dereliction to advantage.

With respect to Shell cashing the pipe line's checks, the fact is that at all times Shell was entitled to receive *at least* the amounts represented by these checks. There is nothing on the checks to indicate that the amounts thereof were to be in full settlement of any disputed amounts which might exist between the parties. There is nothing to show, and it could not have been shown, that Shell accepted these checks in satisfaction of its then active claim. The routine acceptance of checks for an amount admittedly due and owing does not prejudice Shell's right to claim the higher price, nor indicate an intent contrary to the position which Shell has consistently maintained that it felt its price was increased by the February 1954 agreement (R. 17, 18).

As to the auditor's routine confirmation letters, Shell received two of these prior to its October 11, 1954 letter to the pipe line (R. 35-36). The first of these letters is dated January 21, 1954 and was signed by Shell's accountant on January 28, 1954 (Ex. 12, R. 50-51). Since both dates were prior to the contract of February 17, 1954, this letter can have no possible effect in this case. The second letter is dated August 10, 1954, but does not show the date when it was signed by Shell (Ex. 12, R. 51-52). At any rate, the letter was signed by Shell's accountant at a time when Shell's Gas and Legal Departments were in the process of gathering together and considering data necessary to

ascertain Shell's legal position (R. 16, 34). Of the remaining letters, all of which were received during the period the dispute was being negotiated between Shell and the pipe line (R. 16-17), the one dated April 21, 1955, which was signed by Shell on April 27, 1955 (Ex. 12, R. 52-53), notes Shell's exception that the balance shown does not include "our claim for price increase of $.03503 on 7,568,213 Mcf of gas sold from 9/1/53 through 3/31/55" (R. 53).

These letters are no more than routine inquiries being made for information of outside auditors to ascertain whether the pipe line was correctly paying bills which its own records reflected it should have paid. Even had Shell's accountant excepted to all of these routine inquiries, as he did to the one of April 21, 1955, it is doubtful that such exception would ever have come to the attention of the pipe line, as the letters were returned to the outside accountants and there is nothing in the record to show that the pipe line ever had knowledge of Shell's notations thereon. All but one of the letters were signed during the period when the parties were conferring with the view to settling the dispute. Thus, since Shell's position was then well known to the pipe line, and Shell was actively insisting upon its claim to the higher price, it cannot reasonably be said that the signing by Shell's accountant of these routine inquiries constitutes a practical construction by Shell that it thereby construed its price clause as not having been activated by the February 1954 contract. It is obvious that the parties understood that their differences as to the amounts payable under the contract were being held for future determination. See *Kansas Power & Light Co.* v. *Hugoton Production Co.*, 10 Cir., 251 F. 2d 946 (1958).

Shell's accountant, by accommodating the pipe line's outside auditors by confirming to them that the pipe line had credited certain amounts to Shell (like the routine act

of depositing checks for an amount admittedly due), practically all of which took place while Shell was insisting that its price had increased, cannot fairly and reasonably be said to constitute such course of conduct on Shell's part as to amount to an inconsistent practical construction resulting in Shell thereby relinquishing the very claim upon which it was then insisting.

C. Petitioners contend that the Commission's interpretation of the Shell clause furthers the purpose of the Gas Act to protect customers.

This is not a case involving whether a price is unjust and unreasonable under §5(a) of the Act, as was the case in *F. P. C.* v. *Hope Natural Gas Co.*, 320 U. S. 591 (1944); nor is this a case involving the jurisdictional coverage of the Gas Act as in *F. P. C.* v. *Interstate Natural Gas Co.*, 336 U. S. 577 (1949), and *Phillips Petroleum Co.* v. *Wisconsin*, 347 U. S. 672, *supra;* nor does this case involve the question of whether an initial price in a certificate proceeding is in the public convenience and necessity, as was the situation in *The Atlantic Refining Co.* v. *Public Service Commission*, 360 U. S. 378 (1959). This case involved solely what *was* Shell's effective price on June 7, 1954, not whether that price was lawful.[37]

The Commission is without power to establish the initial contractual relationship between a natural gas company and the purchaser of its gas. *United Gas Pipe Line Co.* v. *Mobile*

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[37] Shell has filed for an increase to 16.75¢ per Mcf under the contract involved in this case. That increase has been suspended by the Commission and is being collected by Shell subject to refund with interest. Additionally, all of Shell's jurisdictional prices are subject to a rate proceeding instituted by the Commission under §5(a) of the Act (Docket No. G-9446 *et al.*). Shell's rate increase proceeding regarding the 16.75¢ price has been consolidated with the rate investigation, and the consolidated proceedings are set for hearing on July 7, 1960. Thus consumers are being fully protected under the appropriate sections of the Act (§§4(e) and 5(a)) against unlawful charges.

Gas Corporation, 350 U. S. 332, *supra; United Gas Pipe Line Co.* v. *Memphis Light, Gas and Water Division*, 358 U. S. 103, *supra.*

Since Congress did not invest the Commission with power to fix initially the type of arrangement under which natural gas companies could sell gas, it is illogical to contend as petitioners in effect do, that the Commission could become indirectly endowed with such power through the medium of its interpretation of the contract. The statutory scheme of the Gas Act is amply adequate to safeguard the interests of all segments of the industry and the consuming public. By the rate review powers vested in it under §4(e) and 5(a) of the Act, the Commission is fully empowered to safeguard the gas consuming public against unreasonable charges. There is no warrant in the Act for the Commission to extend its function through the process of construction. In *United Gas Pipe Line Co.* v. *Mobile Gas Corp.*, 350 U. S. 332, 339, this Court said:

> "... (T)he Natural Gas Act permits the relations between the parties to be established initially by contract, the protection of the public interest being afforded by supervision of the individual contracts, which to that end must be filed with the Commission...."

And the Court further observed, 350 U. S. at 341:

> "... These sections [4(d), (e) and 5(a) of the Act] are simply part of a single statutory scheme under which all rates are established initially by the natural gas companies, by contract or otherwise, and all rates are subject to being modified by the Commission upon a finding that they are unlawful."

Clearly, therefore, the function of the Commission in this case was not to make a price for Shell or to test the

lawfulness of Shell's price, but merely to ascertain what Shell's contract price was on June 7, 1954. While we concede petitioners' statement of the purpose of the Act, we deny that the purpose is properly invocable in this case to support the Commission's otherwise unsupportable construction of the Shell clause.

The Issue of Enforceability Which Was Not Reached by the Court of Appeals.

The Court of Appeals decided this case on one of the two issues briefed and argued to it. It assumed that the 1943 Atlantic contract imposed a binding agreement-to-agree on price in each of its last four five-year periods. "Thus", said the Court, "it has not been necessary to determine the several questions raised in connection with the arguments directed to that phase of the case. Of course if the Atlantic contract of 1943 was not a binding agreement-to-agree, that circumstance alone would place the February, 1954 Atlantic contract fully within the terms of the escalation clause in the Shell contract" (R. 165).

Before the Examiner, the Commission, and the Court of Appeals, one of the principal issues was the enforceability and binding effect of the 1943 Atlantic contract as to its last four five-year periods. On that issue, Shell has consistently contended that the law of Louisiana governed because that was the place of performance and the center of gravity of the contract; and under Louisiana law, which follows the civil law of France, a "fixed and determined" price is an absolute essential to the continued binding effect of a "contract *of* sale" or a "contract *to* sell"; and that the 1943 Atlantic contract was clearly subject to a suspensive condition (condition precedent at common law) and hence not a binding or enforceable contract as to each of its last four five-year terms until the contract price for each of those terms was actually supplied *either by agreement of the*

parties or agreement in their behalf by the arbitrators. On that basis, no obligation to sell and to buy gas arose between Atlantic and the pipe line (after the prior price expired on August 31, 1953) until they actually fixed and determined the price in the February, 1954 contract, and the presence of an arbitration clause in the contract does not alter this result. Under Louisiana law the presence of such a clause, like the agreement-to-agree itself, is merely one of the means by which the suspensive condition might be satisfied. This issue was extensively briefed and argued to the Court of Appeals.

In its petition for certiorari in No. 170 (fn. 15, p. 17) the Government states:

> "But while we think there is no doubt of the enforceability of the Atlantic contract, that issue is, we submit, immaterial in any event. The parties treated the contract as binding and complied with it, and it is not for Shell, a stranger to the contract, to say that it is not legally enforceable. . . .
>
> However, even should this Court disagree that the question is immaterial, it would not be required to decide the enforceability of the Atlantic contract. The court of appeals assumed it was enforceable for purposes of its decision, and it is that decision that presents the questions of general importance of which review is sought. Should the Court reverse that decision, it could then—if it considered the question material—remand the case to the court of appeals to determine the enforceability question."

We disagree with the Government that the enforceability question is not material. The Commission and the Court of Appeals thought it was, although the latter did not find it necessary to decide the issue. It is, we submit, very material whether the 1943 Atlantic contract was

enforceable as to its last four five-year periods, because if it was not, the parties clearly made a new contract creating legally enforceable rights and obligations which did not theretofore exist when they entered into the February, 1954 contract. The fact that Shell was not a party to the 1943 Atlantic contract is not a valid basis for saying that Shell cannot look to the status of that contract to determine whether its rights have ripened under its favored-nation clause. The very nature of the clause contemplates that that will be done, otherwise the clause would be a hollow thing with its meaning dependent solely upon what interpretation the pipe line saw fit to give to it.

While we maintain that the enforceability question is very material, we do not urge the Court to pass on that question. Petitioners do not appear to have gone into it except perhaps indirectly in footnote references (see Govt. Br. fn. 22, pp. 49-50; Br. in No. 167, fn. *, p. 24) and, in view of the Government's statement in its petition for certiorari (see above) we shall not go into the various aspects of that issue which includes a question of conflict of laws together with the application of the Louisiana law of sales to the 1943 Atlantic contract. If the Court differs with the Court of Appeals on the issue resolved, we suggest the matter be referred to the Court of Appeals for resolution of the enforceability issue.

Conclusion.

For the foregoing reasons, it is respectfully submitted that the judgment of the Court of Appeals should be affirmed. In the event the judgment is not affirmed, the

matter should be remanded to the Court of Appeals to pass on the question of the enforceability of the 1943 Atlantic contract during its last four five-year periods.

Respectfully submitted,

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April 1960.

APPENDIX A.

Section 19(b) of the Natural Gas Act

[as it appears in 15 U. S. C. A. §717r(b) (Supp. 1958)]

[Rehearings; court review of orders]

(b) Any party to a proceeding under this chapter aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals [*] of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be transmitted by the clerk of the court to any member of the Commission and thereupon the Commission shall file with the court the record upon which the order complained of was entered, as provided in section 2112 of Title 28. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional

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[*] "Circuit court of appeals" was replaced by "court of appeals" by act dated June 25, 1948, effective Sept. 1, 1948 (62 Stat. 869), as amended by act dated May 24, 1949 (63 Stat. 139).

evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in section 1254 of Title 28.

APPENDIX B.

Section 10(e) of the Administrative Procedure Act

(60 Stat. 243, 5 U. S. C. 1009(e))

[SEC. 10. Except so far as (1) statutes preclude judicial review or (2) agency action is by law committed to agency discretion—]

(e) *Scope of Review.*

So far as necessary to decision and where presented the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of any agency action. It shall (A) compel agency action unlawfully withheld or unreasonably delayed; and (B) hold unlawful and set aside agency action, findings, and conclusions found to be (1) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law; (2) contrary to constitutional right, power, privilege, or immunity; (3) in excess of statutory jurisdiction, authority or limitations, or short of statutory right; (4) without observance of procedure required by law; (5) unsupported by substantial evidence in any case subject to the requirements of sections 1006 and 1007 [*] of this title or otherwise reviewed on the record of an agency hearing provided by statute; or (6) unwarranted by the facts to the extent that the facts are subject to trial de novo by the reviewing court. In making the foregoing determinations the court shall review the whole record or such portions thereof as may be cited by any party, and due account shall be taken of the rule of prejudicial error.

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[*] Sections 7 and 8 of the Administrative Procedure Act.

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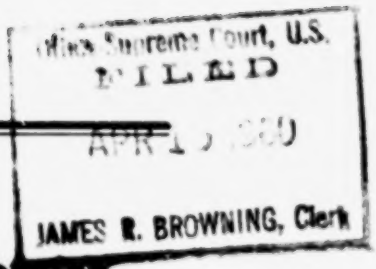

IN THE

Supreme Court of the United States

OCTOBER TERM, 1959

Nos. 167 and 170

TEXAS GAS TRANSMISSION CORPORATION, LOUISVILLE GAS AND ELECTRIC COMPANY and FEDERAL POWER COMMISSION,

Petitioners,

v.

SHELL OIL COMPANY,

Respondent.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

REPLY BRIEF FOR PETITIONERS TEXAS GAS TRANSMISSION CORPORATION AND LOUISVILLE GAS AND ELECTRIC COMPANY

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I *

The Shell brief devotes most of its argument to an attempt to show that the decision of the Commission herein did not involve any question of "industry practice, or economic impact" of favored-nation clauses or other similar question requiring application of the Commission's special expertise (e.g., Shell Br. 28).

In its attempt to establish that the Commission's interpretation of the Shell favored-nation clause was subject to

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* For the convenience of the Court, we have attached a brief chronology of the more important events as Appendix A to this brief.

unlimited de novo review, Shell also seeks to divert the Court by characterizing the Commission's inquiry as to the meaning of the clause as presenting a question solely of law. In support of this claim, Shell states that the Commission interpreted the clause solely on the basis of court decisions and not on the basis of administrative expertise.*

Although the Commission did cite cases in support of its conclusion that the Atlantic price redetermination was not a contract for the purchase of gas, it reached its conclusions as to the meaning of the Shell favored-nation clause by inferring the ultimate fact (the intention of the parties expressed in the Shell favored-nation clause) from the primary facts (the words of the clause and the expression utilized in numerous other favored-nation provisions to which Shell was a party). Whether one chooses to label the question thus decided as one of law or of fact, it remains that the determination made was one peculiarly within the specialized competence of the Commission, which employed its expert administrative understanding of the industry in drawing the inference of ultimate fact.

Shell would have this Court believe that there is absolutely no value to be attached to the continuous contact and exposure of the Commission, since 1938, to the unique and specialized contracts between gas producers and pipelines. Shell tells this Court that any trial court is as competent as the Commission to interpret these instruments. That expertise was involved here is borne out by the egregious

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* Shell does not deny the need for uniformity of interpretation, but urges that it can be obtained through review by this Court (Shell Br. 13-14). As to precedent, Shell brushes off the *Memphis* decision (358 U. S. 103, 114-15), and does not mention *Pennsylvania R. R.* v. *Day*, 360 U. S. 548, 553 or *United States* v. *ICC*, 198 F. 2d 958 (D. C. Cir. 1952), *cert. denied*, 344 U. S. 893 (see our Main Brief, at pp. 13-15). See also *Order of Railway Conductors* v. *Pitney*, 326 U. S. 561, 566-67. A brief indication of the extent of the Commission's accumulated experience is contained at pages 8-9 of our Reply Brief on the petition for certiorari.

fact-finding errors committed by the Court of Appeals. It is also demonstrated by Shell's own brief where it goes on for page after page attempting to persuade this Court of *its* views of the industry meaning of various escalation clauses.*

Thus Shell constantly reiterates throughout its brief that no question of "industry practice or the economic impact of favored-nation clauses" was involved in the case (Shell Br. 28, cf. 36, 37). But Shell, despite these protestations at other points in its brief, gives elaborate expositions of what it understands to be the industry practice (e.g., Shell Br. 44-46).

II

Shell never comes to grips with a major complaint of the petitioners concerning the decision of the Court of Appeals. This is precisely that the Court of Appeals decided the case on the ground that the language of the escalation clause in the Shell contract must be given a special meaning in light of the "usual objective" of such a clause in the "trade" and its business practicalities, whatever its significance would be under ordinary principles of contract law.** There is no doubt whatever that a reviewing court cannot make such findings of fact and of industry practice, since these are exclusively in the province of the expert body.

The error of the Court of Appeals is nowhere better illustrated than in that part of the opinion which is quoted and paraphrased in the following paragraph of the Shell brief (p. 48):

> "The gist of the conclusion of the Court of Appeals is '. . . the fact cannot be avoided that, at

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* See, for example, its arguments about what is and what is not a "typical" price redetermination clause (Shell Br. 18, 44-46), and similarly as to what is the "*usual*" favored-nation clause (33).

** It is doubtless inadvertent but psychologically interesting that when Shell refers, at page 46, to this passage of the Court's opinion, it omits the qualification made by the Court in the words "in the

> least for purposes of the favored nation clause, the "entering of a contract for the purchase of gas" has not been accomplished until the price has been established' (R. 164); and '. . . while there may have been enforceable means for settling the rate of payment in the event the parties could not agree, it would nonetheless be true that it was when the price was finally established, *by whatever means*, that a contract had thereupon been entered' (R. 164)." (emphasis theirs)

As Shell recognizes in the above quoted passage of its brief, the Court of Appeals said that "at least for purposes of the favored nation clause" the determination of a price under the Atlantic contract must be regarded as entry into a contract, no matter how that price was determined and no matter that neither of the parties to the Atlantic contract in connection with such determination did anything that could be remotely described as entering into a contract. For if a price were found pursuant to the arbitration provision of Condition XII of the Atlantic contract, the agreement and consent of the parties whereby that price would be able to be determined and whereby that price would become binding upon them would be the agreement and consent they gave at the time the original contract was entered into, since they would have given no other.

The Shell argument, as this analysis makes apparent, gallops furiously in opposite directions. On the one side, Shell's brief stridently insists that there is no special art involved in the construction of the Shell contract escalation clause and that it must be construed according to ordinary contract principles as any ordinary privately negotiated contract would be construed. One hundred and eighty degrees in the opposite direction it insists with equal vigor that the Atlantic contract, and what was done

under it, must be given a special significance "at least for the purposes of the favored nation clause."

The Court of Appeals reaches the same result with respect to the actual agreement of the parties to the contract pursuant to its provisions as it does with to a determination of price by arbitration. For the Court of Appeals, having said that the agreement of the upon price constituted entry into a contract for the of gas, immediately goes on to say that in reaching decision it has assumed a "binding agreement on the price."

Again it seems clear that if the agreement of the ties as to price was made pursuant to a binding agreement to agree, then the contract was made and entered into whenever the parties entered into the "binding agreement agree." In this case—when the original Atlantic contract was entered into.

The plain fact of course is that the provisions of Section III of the Atlantic contract imposed a binding obligation upon the parties to that contract as to the price to be paid for gas throughout the life of the contract. Neither party could by unilateral action relieve itself of these obligations. These are the "realities" of the situation to which the learned court below paid only lip service in reaching its decision.

III

Shell is equally inconsistent in another aspect of its interpretation of the escalation clause of the Shell contract. On the one hand Shell contends vigorously that the words used in its contract were used in "an ordinary, non-technical sense" (Shell Br. 23) and that it "speaks for itself in clear ordinary language" (Shell Br. 35). On the other hand, Shell argues by quotation with emphasis from the testimony of its own witness Orine that the meaning of the

escalation provision should be determined on the basis of the understanding of Quinn and his associates at Shell as to what it meant when they entered into the contract containing it (Shell P.. 40).

If Shell is right in its contention that the terms of the contract are clear and unequivocal, then under familiar principles that fact itself bars resort to parol evidence to construe it.

In any event, even under the most liberal principles permitting parol evidence to be used in the construction of contracts, evidence which consists only of the unilateral understanding of one party to a contract as to what it means with no showing that that understanding was communicated to the other party, is completely inadmissible.*

Nevertheless, the learned court below cited this testimony and, transmuting the unilateral understanding of the Shell witness to the "intention of the parties", found that it tended strongly to support the construction which the court made of the clause.

It is our position that the language of the escalation clause of the Shell contract was sufficiently clear on its face and sufficiently usual in the practice of the industry to permit the Commission authoritatively to interpret it against the background of the Commission's long experience and expertise without reference to parol evidence. If parol evidence of the intention of the parties were necessary, however, to a proper interpretation of the contract, then we sub-

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* Actually, when the testimony of the witness Quinn is considered in its industry context, his professed understanding of the escalation clause does not coincide with the position now contended for by Shell. His testimony as to the favored-nation clause made no reference to increases based upon "negotiated agreements." That testimony rather referred to increases to the "going price, the market price" (R. 14). This may well have been a reference to *prices under new gas purchase contracts.*

mit the record before the Commission was wholly inadequate to support the construction adopted by the Court below.

IV

On the subject of the redetermination of price under the Atlantic contract, Shell is unable to make the argument it makes except by ignoring the plain facts of record. Thus, Shell argues in its purported statement of the facts of the case that the Atlantic contract did not specify a workable formula for the redetermination of price and that what the parties did in 1953 and early 1954 was to bargain and, in effect, to "horse trade out" an agreed price (Shell Br. 9-10).

In this connection, Shell cites and quotes the testimony of the witness Bowser of Atlantic who was called as a witness by Shell. What Shell omits to mention is that the context of Mr. Bowser's testimony shows that the negotiations between Atlantic and the pipeline company were not aimed at reaching agreement on price as such. Rather, they were aimed, according to the express understanding of both parties to the negotiations, at reaching agreement upon the application of the standard for price determination prescribed in Article III(b) and (c) of the Atlantic contract.

This standard was "prevailing prices for gas being sold in similar quantities in the southwestern part of Louisiana" (R. 86). The witness testified that the parties to the redetermination would be bound by agreement between them as to the "prevailing prices." As he put it: ". . . if we agreed on a prevailing price, I think that would be it" (R. 24). He further testified that the only dispute between the parties was as to the application of this standard. As he put it "We said one thing was the prevailing price and they said something else was" (R. 24).

Doubtless Shell has omitted these statements from its carefully selective quotation of Mr. Bowser's testimony in order to avoid the effect of those authorities such as *Brassert* v. *Clark*, 162 F. 2d 967, 971-72 (2d Cir. 1947) (Hand, J.). These hold that a standard for the determination of price of this character is definite and binding upon the parties even though there may be disagreement as to the application of the standard in a particular factual situation.*

It appears that the Court of Appeals was misled by the shorthanded verbalisms used by the parties such as "negotiations", "haggling", and the like, into overlooking what they actually did. The undisputed facts of record show that the so-called negotiations were really a species of fact finding. This is demonstrated not only by the above testimony of Bowser but also by the contemporaneous written record of what the parties did. Thus, the record shows that they exchanged elaborate tabulations intended to be evidentiary of the fact upon which they were seeking to agree, *i. e.*, prevailing price in southwest Louisiana (Exs. 5, 6, 7; R. 38-45). The "agreement" of February 1954 was in effect a stipulation between the parties as to the fact. Once this fact was determined, price was fixed under the contract as automatically as it would have been under any "settled step-up in price".

Indeed, the price redetermination provision of the Atlantic contract is not essentially different from the type of price redetermination provision contained in the Shell contract which apparently both Shell and the Court of Appeals con-

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* It is well settled that construction of the contract by the parties thereto removes any possible indefiniteness and clarifies any ambiguity, and is binding upon them. See, e.g., *Col-Tex Refining Co.* v. *Coffield & Guthrie, Inc.*, 196 F. 2d 788, 790-91 (5th Cir. 1952). Accordingly, the parties to the Atlantic contract having treated the price redetermination provisions as binding obligations, those provisions are fully enforceable.

cede could not trigger the escalation clause. Shell attempts to maintain this point by contending that in the Shell contract type of price redetermination clause, the redetermination is "gauged by a definite formula to be calculated by simple arithmetic computation" (Shell Br. 45). The Atlantic contract provision by contrast, Shell asserts, is "unique and nondescript" and provides that the parties agree on the "contract price" (Shell Br. 45). But this analysis overlooks the fact that both clauses constitute assent to a change in price, automatically controlled by the operative fact, once determined or agreed upon. Further, despite Shell's talk of "simple arithmetic computation" each of the provisions assured certainty by providing specifically for arbitration in the event that the parties are "unable to agree" on price under the prescribed standard. (Shell Contract, Item A, R. 67; Atlantic Contract, Item E, R. 86)

In this phase of its argument Shell appears stubbornly determined to adhere to its denial that the Atlantic contract contained a price redetermination provision by simply ignoring anything in the record to the contrary. Illustrative is Shell's treatment of the letter by which the pipeline company invited Atlantic to commence negotiations looking to agreement on the application of the standard for price determination prescribed in the contract. Shell quotes this letter as evidencing willingness on the part of the pipeline company "to commence negotiations with you [Atlantic] concerning such price" (Shell Br. 9). Actually, the sentence immediately preceding the one thus partially quoted by Shell states correctly of the contract "Paragraph (c) of Article III of the original contract provides for *price redetermination* for each five year period." (Ex. 4; R. 36-37) (emphasis supplied).

Shell's insistence that the Atlantic contract did not contain a price redetermination clause carries it to the extreme

of stating at page 43 of its brief "The Atlantic contract does not contain a price redetermination clause nor did the Commission so hold." It is difficult to see how Shell can make this statement in the face of the plain language of the majority opinion of the Commission which prefaces quotation of paragraphs (b), (c) and (d) of Condition III of the Atlantic contract with the statement that "The contract provided for price redeterminations after the end of succeeding five-year periods in the following language . . ." (R. 131).*

Implicit in Shell's contention is the admission that if the provisions of Condition III of the Atlantic contract were in fact a price redetermination provision, compliance therewith by the parties to the contract would not constitute entry into a new contract sufficient to trigger the escalation clause of the Shell contract.

In further pressing its contention that the Atlantic contract did not contain a price redetermination provision, despite the record and the holding of the Commission to the contrary, Shell advances the unique argument that price redetermination as used in the industry does not connote normal meaning of the word but rather must be taken as limited to a revision of prices by way of increase. The answer to this suggestion is that if the term price redetermination has any special significance in the natural gas industry, this is a matter clearly falling within the special competence and expertise of the Commission. The Commission having found that the Atlantic contract does contain a price redetermination provision, under settled principles of judicial review that determination should

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* Lest there be any doubt, Shell specifically argued to the contrary in its Application for Rehearing before the Commission (R. 140), which was denied by an order which continued to refer to "price redetermination" (R. 145-46).

not be disturbed by the court absent a clear showing that it was erroneous in law or unsupported by the evidence in the record before the Commission.*

Not only is there no such showing here, but, in fact, the evidence in the record demonstrates unequivocally that the parties regarded the Atlantic contract as containing a provision for price redetermination according to a specific standard. They did in fact make their determination of price on the basis of such standard.

V

Perhaps the most egregious example of the false premise upon which the bulk of the Shell arguments rests is Shell's constant disregard of the plain language of the escalation clause, which requires that Texas Gas enter into a "contract providing for the purchase by it of gas".**

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* Shell apparently agrees that expertise in the natural gas industry is necessary to the proper interpretation of a price redetermination clause but prefers the expertise of the anonymous (so far as this record is concerned) author of a bill in Congress to that of the Commission (Shell Br. 45-46).

** Shell's brief somewhat muddies the waters by stating that petitioners claim that the favored-nation clause could be triggered only by entry into a contract for the supply of new gas. While clearly such a contract would trigger the clause, and we have so stated, we also agree that any contract entered into after 1951 and hence "new" would have the same effect (*cf.* Shell Br. p. 20, lines 2 to 5) so long as it was a contract "providing for the purchase of gas" under which the price is "higher" (after due consideration is given to various factors as required by the favored-nation clause). Similarly, both Shell and the Court of Appeals by-passed the terms of the rate schedule *which are really in issue here*—the requirement of entry into the post-1951 contract for the purchase of gas—by talking at large about a unitary purpose for all favored-nation clauses generally, regardless of differences in provisions, and never about the purpose of the future contract requirement. Shell's attempt to argue that there is some kind of "gap" or "void" (Shell Br. 18-19, 41-42) is merely another way of disposing of the future contract requirement. There is absolutely no "void". Shell gets exactly the price agreed upon continuously until Texas Gas enters into a post-1951 contract for the purchase of gas in the area at which price

The fact is, of course, that Shell is able to make the argument it makes only by ignoring the fact that the escalation clause of its contract required the entry by Texas Gas into a contract providing for the purchase of gas. Such a contract, as the language of the escalation clause itself explicitly recognizes, requires terms, not only as to price, but, as well, as to quality, quantity, methods of delivery, and the like. Under no conceivable interpretation can it be said that the February 1954 letter passing between Atlantic and Texas Gas contains any such terms, or even makes reference to any such terms.

The best that Shell can say on this point is to cite the *American Colortype Co.* case (Shell Br. 17-18, 19 and 49) and to suggest that the parties could have scrapped their original contract with its multifarious detailed terms and conditions as to quality, quantity, methods of delivery, etc., and entered into a wholly new contract in which they might have adopted by express reference some or all of the terms of the abandoned contract. The short answer to this suggestion is that that is not what the parties actually did.

In sum, the escalation clause of the Shell contract is not triggered by entry into a "contract", but only by entry into a "contract providing for the purchase . . . of gas." It is plain that the parties to the Atlantic contract did not, after 1951, enter into a "contract" in any sense. Equally plain is it that whatever they did they did not enter into a "contract providing for the purchase . . . of gas." * Accordingly, the Shell clause was not triggered.

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* The two points are actually the same. The parties did not enter into a post-1951 contract in any sense precisely because their pre-1951 contract was a "contract providing for the purchase of gas" which was complete in all respects, including compulsory means of determining price.

Conclusion

For the reasons stated in petitioners' briefs, the decision and judgment of the Court of Appeals should be reversed and vacated, and the order of the Commission should be affirmed.

Respectfully submitted,

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APPENDIX A

Chronology

For the convenience of the Court, set forth below is a brief chronology of the more important dates referred to in the briefs:

September 1, 1943....	Date of gas purchase contract between Atlantic and Government (Item E; R. 81).
May 11, 1949.....	Assignment of Atlantic contract from Government to Texas Gas (Item H; R. 105).
May 1, 1951.....	Shell and Texas Gas enter into new gas purchase contract (Item A; R. 57).
February 17, 1954....	Atlantic and Texas Gas redetermine price under 1943 contract for period September 1953 to August 1958 (Ex. 9; R. 46).
March 1954	Shell learns of Atlantic price redetermination, but makes no claim of escalation (R. 16).
June 7, 1954.....	Date of Supreme Court's *Phillips* decision re regulation of independent gas producers. FPC subsequently (in July) adopts regulations for independent producers.
October 11, 1954.....	After FPC regulations announced, Shell first raises with Texas Gas claim of escalation (Ex. 2; R. 35).
November 18, 1954....	Shell submits June 7, 1954 rate schedule to FPC, with artificial, sample "bill" showing 12.5¢ rate (Item C; R. 80).

January 6, 1955.....	FPC refuses to accept Shell's sample "bill" as justification of initial rate higher than 8.997¢, and asks for a statement of the basis for Shell's claim (R. 151).
February 11, 1957....	Shell first explains to FPC basis of its claim to a higher initial rate while filing for change in rate to 16.75¢ (Item B; R. 74-75).
March 13, 1957.....	FPC accepts Shell contract for filing as rate schedule, but orders hearing to determine June 7, 1954 initial rate (R. 110).